THE RISE AND FALL OF THE GOLD STANDARD

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by

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FOREWORD

A VISIT to Shaw's latest play has convinced me of my temerity in venturing to address sundry Rotary Clubs on "The Gold Standard," and in expanding the address into the present volume. An amusing passage of the play expresses the absurdity of expecting even the Prime Minister to understand the mystery of the Gold Standard. And yet the clue to the mystery is simple. It is the clue to the mystery of Sairey Gamp's imaginary friend, Mrs. Harris. Briefly, "there ain't no sich standard."

A metal of varying value is incapable of being an accurate standard of value or of currency. Under skilled supervision, and in favourable circumstances, it may provide a medium in which a standard of currency is fixed and maintained. But it is the fixed value, and not the metal, which is the standard of currency.

There have been four highly differentiated systems of currency which have been mistakenly included under one designation "The Gold Standard" during the past hundred years. First there was the international, exchange-stabilising, sterling standard, in operation prior to the War. After the War, the national, price-stabilising, dollar standard operated from 1920 to 1925. From 1925 to 1933 there was an intense conflict of divergent currency standards, competing with each other for supremacy. There remains the hoarding standard now in operation on the Continent of Europe.

Extreme confusion is caused by the misleading assumption that these four systems of currency had one common standard, the Gold Standard.

The Report of the Macmillan Commission is largely to blame for this confusion. Having demonstrated that the historic gold standard had disappeared with the War, and that the industrial disasters from which the world was suffering were due to the extreme inefficiency of the system of currency then in actual operation, it recommended a drastic currency revolution which would substitute a Price Index for gold as the standard of value. But it failed to carry conviction by suggesting that this revolution could be effected by means of rosewater and soothing syrup. Its outstanding achievement was its demonstration of the pretentious hollowness of "The Gold Standard" by proposing both its retention and its abolition. Not only were Prime Ministers and Chancellors of the Exchequer befogged by the resulting confusion. It ultimately brought the World Economic Conference of 1933 to naught.

There is no reason why the ordinary reader should find the realities behind the fiction of the Gold Standard beyond his comprehension. Every trader would resent a claim by his banker to limit the amount of capital he employed in his business. Yet that is precisely the claim of the banking system with respect to the world's commerce and industry under the Gold Standard. It limits the amount of currency available by the arbitrary and irrelevant consideration of the amount of gold remaining after the panic hoarding of

the less progressive nations of the world has been satisfied.

My thanks are due to Messrs. Macmillan & Co. for permission to utilise the quotations from the works of Mr. John Maynard Keynes, of which I have availed myself. My indebtedness to Mr. Keynes for a clear insight into the reactions of currency and industry on each other is unlimited.

C. M.-W.

January 24th, 1934.

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CHAPTER I

CURRENCY STANDARDS

The Gold Standard Fallacy

THE term "The Gold Standard" embodies a fallacy, one of the most expensive fallacies which have deluded the world. It is the fallacy that there is one particular gold standard, and one only. There are innumerable possible gold standards. The assumption that the widely divergent standards of currency masquerading under the name of the gold standard are identical has recently brought the world to the verge of ruin. Britain went on to a gold standard in 1925 under the delusion that, because it bore the designation of "the gold standard," it was identically the same as the gold standard from which she had been forced by war in 1914. Seven long years of depression and disaster, and a very narrow escape from ruin, was the price paid for this delusion. Other manifestations of the fallacy are the repeated declarations of loyalty to "the gold standard" and resolutions in favour of the "restoration of the gold standard" which are so frequently made as a concession to the unthinking and the orthodox. The fact that the gold standard

which it is desired to restore is, according to the declarations, to be something vitally different from any gold standard which has previously operated, does not appear to reveal the truth that there is not one, but that there are many gold standards.

The fallacy is due to loose thinking as to what a standard of currency actually is. A standard of currency is a standard of value, and a standard of value must be a fixed unit of value. It cannot possibly be a metal or a fixed weight of metal. It may be the value of a fixed weight of metal, provided that due care is taken that the value selected is so fixed that it cannot be effected by the law of supply and demand. Gold was chosen by Britain in 1816 to be the metal whose value was fixed as the standard of currency largely because of this consideration. Its value could be fixed, and kept fixed, with less trouble than with any other metal. As a matter of fact Britain succeeded in keeping the value of gold at the fixed value of £3 17s. 10½d. per ounce for eight years short of a century, from 1822 to 1914.

Previously, silver had provided the standard of currency. But it had never been a true scientific standard. The silver standard was not a value, but a weight, the weight of an ounce of silver. In his pamphlet published in 1730, Conduitt, the successor to Sir Isaac Newton as Master of the Mint, stated that "an ounce of fine silver is, and always has been, and ought to be, the standard and invariable measure between nation and nation." But the value of an

ounce of silver was not fixed. It varied from year to year. It varied from country to country. It fluctuated in value not only relatively to gold, its rival as a currency metal, but also relatively to the value of the silver coinage. Instead of being a fixed and stable unit of value, the only possible basis for a scientific currency standard, it was variable and fluctuating. The irrelevant quality, the weight of the unit, was fixed. The relevant quality, its value, was not fixed. The silver standard was an illogical attempt to base a standard of value on a fixed unit of weight. As such it was a source of perpetual confusion and of currency instability.

The nature of this defect of the silver standard can be illustrated by a reference to the physical standards of length, weight, and capacity. The unit of length is the yard, carefully and meticulously defined as the distance between two gold plugs set in a platinum bar, fixed in a wall of the Houses of Parliament, and measured at a temperature of 62 degrees Farenheit. The standard of length, the yard, is accordingly a fixed unit of length. So the standard of weight, the pound, is a fixed unit of weight, and the standard of capacity, the gallon, is a fixed unit of capacity. The silver standard, being a fixed weight and not a fixed value, was a false standard of value. It lacked the prime essential of a standard, that of fixity or stability in the quality it purported to measure.

This error was rectified when Britain transferred

to a gold standard in 1816. The great merit of the gold standard was its logic, not its gold. It was not merely a slavish copy of the silver standard in a more resplendent metal. The currency revolution effected by Britain in 1816 was much more fundamental than a mere transfer from silver to gold. It was a transfer from a false and fluctuating standard, to a fixed and scientific standard. The transfer was from a weight of silver to a value of gold.

The decision having been made that the future standard of currency was to be a fixed value, the pound sterling was the obvious connecting-link between the two standards, the old and the new. The pound sterling had hitherto been a silver value, the value of twenty silver shillings. It had now to be transferred not only into a gold value, but into a fixed gold value. The fixed gold value selected was that which happened to be the Mint price of gold at the last previous coinage of guineas, £3 17s. 10½d. per ounce. Experience had proved that 22 carat gold, that is gold eleven-twelfths fine, was the most durable alloy for a gold coinage. At the fixed value of gold adopted for the new standard, the pound sterling, was the value of 5 pennyweights 3·274 grains of gold, eleven-twelfths fine. In the resolution introducing the legislation of 1816, this weight of gold was equated to the value of twenty silver shillings, or the pound sterling, and became henceforth the standard of the British currency. Britain adopted, in fact, the sterling standard.

The value of gold adopted for the new standard, £3 17s. 10½d. per ounce, was not the natural and inherent value of gold. The value of gold, like that of every other commodity, is governed by the law of supply and demand. Had the value of gold adopted for the standard been £4 per ounce, or £3 15s. per ounce, the result would have been a gold standard of a different nature. The value actually adopted was that which equated gold with the pound sterling. Of the numerous gold standards which might have been adopted, the particular standard selected was that which transformed the old variable silver value of the pound sterling into a fixed value of gold. It is therefore incorrect to say that in 1816 Britain went on to "the gold standard." She went on to "a gold standard." As the actual standard adopted was specially designed to equate the value of the pound sterling on the old standard with its value on the new standard, the correct designation of the new standard was "the sterling standard." It was the spectacular nature of the transformation from silver to gold which caught the eye. The real nature of the transformation, from an illogical standard of weight to a scientific standard of value was appreciated only by the expert. In popular estimation Britain had transferred from silver to gold, and "the gold standard" though scientifically incorrect, was the designation universally applied to the new standard of currency.

Apart from the various possible gold standards,

based on the selection of different values of gold for the unit of value, there were other possible gold standards, based on fundamental differences in methods of management or objectives of control. The possibility of such different gold standards is best appreciated from the following passage from the evidence of Dr. Miller, a member of the Federal Reserve Board, in his evidence to the United States Congress Committee on Stabilisation:—

> The gold standard means more than a legal undertaking to redeem the currency and credit of a nation in gold . . . the gold standard means a set of practices, a system of procedure, never formulated, never consciously thought out, not invented by anybody, but the growth of experience of the great commercial countries of the world, rather than merely the employment of gold to redeem all forms of obligations.

Judged by this criterion, the currency standard of the United States which operated from 1914 to 1925, diverged widely from the sterling standard of currency which had operated from 1816 to 1914. The American "set of practices," the American "system of procedure," essential factors in determining the nature of a currency standard, were vitally different from the British practices and the British procedure of the sterling standard. Moreover, the value of gold on which the currency standard from 1914 to 1925 was based was not the sterling value of £3 17s. 10½d. per ounce.

Unfortunately, investigations into the nature of currency standards are in a backward stage, and no

distinctive terms have been established to distinguish between the pre-war sterling standard and the international currency standard, under the management of the United States, which succeeded it. They were both described under the misleading and fallacious designation "The Gold Standard." They were both gold standards, but they differed so fundamentally in their basic unit of value, their method of operation, and their aims and objects, that the absence of distinctive names for them was the source of endless confusion. It was under the illusion that the currency standard managed by the United States in 1925 was identical with the sterling standard that Britain joined the former. For convenience, the international currency standard operating from 1914 to 1925 may be called the Dollar Standard, to distinguish it from the currency standards which preceded it and which succeeded it.

It is difficult to find any term to define the absence of system produced by the conflict of British and American currency principles and practices which commenced in 1925. The confusion was intensified in 1928 by the entry of France with a heavily devalued currency, a strong hoarding complex, and an intensely national conception of the operation of an international currency. Other countries joined the conflict, and each added its quota to the confusion. The struggle for supremacy was, however, between the policies of Britain, France, and the United States.

Each of the three principals claimed to be on the

gold standard, each claimed that its own principles and practices were in conformity with those of the historic gold standard. Of the three, Britain only showed any consciousness that a fixed value of gold, and not gold itself, must be the basis of any currency standard. But the erratic and unaccountable workings of the system, and the wildly fluctuating commodity price of gold, distracted attention from what had been the bedrock of the sterling standard, the fixed price of gold, and effectually submerged the true faith. France and the United States frankly operated the system as if gold itself was the standard, just as in the eighteenth century, the weight of an ounce of silver, whatever its value, had been the standard. A superstitious belief prevailed that gold, merely because it was gold, would assure the success of any currency to which it was linked in value. The superstition arose from the fallacy that there was a specially efficient basis of currency known as "the gold standard." Fallacious as the term may be, devoid of all meaning as it is, "The Gold Standard" is the only designation capable of describing the conflict of policies that proceeded under its name from 1925 to 1931.

It is recognised that the adoption of the terms "the sterling standard," "the dollar standard," and "the gold standard" as the designations of the international currency standards, operating during the periods 1816–1914, 1914–25, and 1925–31 respectively, is an innovation. But it is an innovation which helps

to simplify a most complex problem. One of the main difficulties which the ordinary business man finds in understanding what is meant by "the gold standard" is that the term comprises so many contradictory meanings. The confusion is most apparent in the Report of the Macmillan Commission. Having to apply the same term "the gold standard" to standards of a widely divergent nature, it was reduced to the pretence that the differences were merely chronological. Fundamental divergences were introduced under such complementary phrases as: "before the war" and "since the war"—"formerly" and "in actual fact to-day"—"the nineteenth-century philosophy of the gold standard" and "the modern post-war world" —"the classical theory of the gold standard," and "in the modern world." These chronological phrases are employed to denote not differences in time, but divergencies in principles, policies, practices, procedure, and philosophies. The report would have gained greatly in lucidity if these divergencies had been described under different names, and not all grouped together under one unmeaning designation, the gold standard.

In addition to simplifying a complex problem, it is possible that the recognition that there are many possible variants of the gold standard, widely divergent in their characteristics and operation, may induce some attempt at precision when in future any declarations in favour of a "restoration of the gold standard" are made. Up to the present, such declarations have

been so vague as to be unmeaning. They are negative and nebulous, instead of being positive and informative. No declaration in favour of the restoration of the gold standard is of the slightest value unless it states the nature of the currency stabilisation it is desired to establish, the respective importance to be given to stability of prices and stability of the exchanges, and the exact nature of the unit of value to be selected as the currency standard. Unless such particulars are given, and unless they are accompanied by some description of the measures by which the gold unit of value is to be kept stable, they may be regarded as tributes of superstitious reverence to an institution that has departed. Indeed, the many conditions and qualifications with which a declaration in favour of a restoration of the gold standard is usually accompanied, render it more of an epitaph than a confession of faith.

CHAPTER II

THE SILVER STANDARD

The Pound Sterling

THE history of the British monetary system revolves round the pound sterling. The term "Sterling," or Easterling, dates from the Norman Period. It was first used as a term to describe the silver penny. When a gold coinage was introduced, its meaning was enlarged. In its singular form it still denoted the silver penny, but in its plural form, "sterlings," it meant the silver coinage generally.

The term "pound sterling" first appeared in the form of a "pound of sterlings," meaning a pound weight (troy) of silver pennies or of silver coinage. The meaning was gradually associated with the value of a pound of silver coins, rather than with its weight. In the course of years the value gradually depreciated, and it was divorced from the weight of a pound. It became the pound sterling, a value, instead of the "pound of sterlings," a weight.

The principal coins which survived the Wars of the Roses were the silver coins, the penny and the groat (4d.), and the gold coins, the noble and the angel. The noble had originally been of the value of 20 groats or 80 pence. But at the time of the accession of Henry VII it had appreciated to the value of 120 pence. The angel was a new gold coin introduced to

take the place of the noble at the value of 20 groats or 80 pence.

The modern coins, the shilling and the sovereign, were introduced by Henry VII, the first—and the greatest—of the Tudor monarchs. The previous coinage system, the noble, the angel, and the groat, did not fit in well with the national system of keeping accounts. The pound sterling, although it was not represented in the currency by any coin, had established itself as the principal unit in the system of accounts. Neither the noble, the angel, nor the groat were convenient fractions of the pound sterling for accounts purposes. The shilling, of the weight of 144 grams of silver, was accordingly introduced, in weight and value equal to twelve silver pennies, and the pound sterling was fixed, and remained for three centuries, at the value of twenty silver shillings. The familiar £ s. d. system of accounts was introduced with the same proportions, 240 : 12 : 1, which still survive.

Hitherto it had not been considered necessary to have a gold coin corresponding to the principal money-of-account, the pound sterling. Twenty shillings was a very high denomination for a coin to circulate in the poverty-stricken England which emerged from the Wars of the Roses. Still it was thought that the time had arrived for the pound sterling to be represented by an actual coin. A magnificent gold coin, 240 grains in weight, was accordingly issued in 1489, equal in value to the pound sterling. As silver was

the standard of the currency, and as the gold coins were only passengers in the system, the new coin was not given the name of the pound, although it was issued to circulate at the value of the pound sterling. The pound sterling was a silver value, and as gold coins shewed a tendency to depart from their silver value, the new gold coin was called the sovereign, to distinguish it from its silver equivalent.

From the first, the sovereign, like the noble and the angel, refused to stay fixed at its nominal silver value. The three gold coins proved a very difficult team to manage. They would not keep in step with their silver values. Partly owing to fluctuations in the relative values of gold and silver, and partly to depreciations of the silver coinage, all the gold coins appreciated in value. The noble climbed up to 11s. 3d. and subsequently to 13s. Further issues then ceased, and it gradually dropped out of circulation. The angel also rose in the world with increasing value but diminishing numbers. It was still in circulation in 1662 when the guinea was first introduced. One reason why the noble and the angel lost favour was the fact that they were odd values relative to the shilling, which grew rapidly in popular favour and importance. The gold crown of the value of five shillings, took the place of the noble and the angel for small transactions for which the sovereign was of too high a value. Successive reductions in its weight kept its value steady in relation to silver at its original value of five shillings.

The sovereign increased gradually in value until in 1558, at the accession of Queen Elizabeth, it was worth thirty shillings. The refusal of the sovereign to keep in step with the silver coinage induced the Government to try a new departure and to make a serious attempt to issue a gold coin of the value of the pound sterling, and to fix it permanently at that value. With this intention they determined to call the new coin a gold pound, to signify that it was to be kept at a constant value with the pound sterling, the value of twenty shillings.

The gold pound weighed 200 grains as compared with the sovereign of 240 grains. For sixty years the Government attempted to keep the gold pound in circulation at the exact value of the pound sterling, and then abandoned the attempt. Like its predecessors, the noble, the angel, and the sovereign, it continually showed a tendency to appreciate. But the moment it attained a value slightly above twenty silver shillings, its value was brought down by the simple expedient of lessening the weight of new issues. During the sixty years in which the gold pound circulated (1544–1604) its weight was brought down by successive reductions from 200 grains to 171 grains, and even then its value had gone up to thirty shillings.

The repeated failures to keep a gold pound in circulation at the silver value of twenty shillings led to the abandonment of the use of the term "pound" for a gold coin. The pound reverted to its previous

meaning of the pound sterling—that is, a money-of-account of the value of twenty silver shillings, and retained that meaning for two centuries, till 1797.

One of the causes of the constant variations in the relative values of silver and gold, tending to make the value of the gold coins diverge continually from their silver value, was the great influx of the precious metals following the Spanish and Portuguese conquests in America. They percolated into Britain through the normal channels of trade with France, Spain, Portugal, and the Low Countries. But a more prolific source of supply was the plunder of the Spanish treasure ships brought to England by the Elizabethan privateers. The additions to the currency through the second source of supply were irregular and capricious, and they caused great fluctuations of value both in the prices of commodities and in the relative values of silver and gold.

The earliest supplies of the precious metals in the form of plunder were succeeded by more regular supplies when the mines of Peru, Brazil, and Mexico were developed under European supervision. So great were the supplies that they caused a severe inflation of all the currencies of Western Europe. It is a fallacy that currency inflation is a disease due to the over-issue of paper money. Inflation is an over-supply of money in relation to the sales and purchases it has to finance. It is just as possible to have an inflation of metallic money as of paper money. Inflation is a disease of quantity not of material.

The period of currency inflation in England, due to the abnormal influx of gold and silver, extended for a period of about a century; from the accession of Elizabeth (1558) to the accession of Charles II (1660). So great was the inflation that the value of the precious metals sank during this period to one-third of their original value. In other words commodities in general were three times as dear. As silver was being produced at a very much greater rate than gold, the depreciation of silver was greater than that of gold. Hence the constant tendency of the gold coinage to increase its value relatively to silver.

The efforts to have the money-of-account, the pound sterling, represented in the coinage by a gold coin of the designation of the pound ceased with the accession of James I. No further gold pounds were issued, and in their stead a new gold coin, the unit or unite, so called to commemorate the union of the crowns of England and Scotland, was issued in 1604. In order to equate it with the pound sterling, its weight was reduced to 154 grains. Like all its predecessors, it gradually increased its silver value, climbing up to £1 2s. by 1610, and it continued to climb throughout the reign of James I.

It had diverged so far from the pound sterling that it was superseded in the reign of Charles I by the broad, at the lower weight of 140 grains. In turn this was superseded by the guinea in the reign of Charles II. The guinea was so-called because the gold from which it was coined came from the Colony

of Guinea. It was intended to equate with the pound sterling of twenty silver shillings, but following numerous precedents, it rapidly appreciated above that value. The career of the guinea is so full of romance and adventure that its story is reserved for another chapter.

The magnitude of the variation in the values of gold and silver in the one hundred and seventy-three years elapsing between the first issue of the sovereign (1489) and the first issue of the guinea (1662) can be estimated from the fact that the weight of the gold coin, issued to circulate at twenty silver shillings, had been reduced from 240 grains to half that weight. Part of this variation was due to a reduction in the weight of the silver coinage, but in the main it represents an increase in the value of gold relatively to silver. A whole series of coins, the sovereign, the gold pound, the unit, the broad, and the guinea, had all been issued with the intention of having the principal money-of-account, the pound sterling of twenty silver shillings, represented by an actual coin in circulation, and the intention had been frustrated by their continuous appreciation in value.

At the accession of Charles II, the currency generally was in a bad state of depreciation, principally as the result of the Civil War. Moreover, prices had risen, and wealth had increased so remarkably during the past century that the old coinage was inconvenient in many respects. Prices had increased three-fold, wealth had increased seven-fold, and foreign enterprise had increased fifty-fold. The broad and the

crown both needed revision owing to their tendency to depart from their silver valuation. The broad, as previously stated, was superseded by the guinea; and the crown was transformed from a gold coin to a silver coin of the same value, five shillings. The new silver crown was most favourably received. Its impressive weight and appearance added greatly to the prestige of the silver coinage.

The general restoration of the silver coinage was, however, postponed till towards the end of the century. The new silver crowns had drawn attention to the extremely depreciated character of the shillings, sixpences, and groats in circulation. In 1696, the restoration of the silver coinage to standard weight was undertaken under the personal supervision of the mathematician and philosopher, Sir Isaac Newton, Warden, and subsequently Master of the Mint. Macaulay's brilliant description of this financial event is still unsurpassed. He makes a long and tedious financial operation stand out as if it were a thrilling romance. Reduced to figures, the coins called in were valued at £5 millions sterling. They were deficient in weight below their true standard weight to the extent of £2 millions in value. The value of the coins re-issued was £7 millions sterling.

Throughout the Tudor and Stuart periods the English currency was on a silver standard. This is authoritatively expressed by Conduitt, Newton's successor at the Mint in the terms, "an ounce of fine silver, is, and always has been, and ought to be, the

standard and invariable measure between nation and nation." The gold coins were merely "passengers," issued for the convenience of the wealthy and to facilitate the wholesale transactions of merchants. They came and they went, as their value diverged from the principal unit of the silver standard, the pound sterling.

In the course of the two centuries herein briefly reviewed, the career of the pound sterling demonstrated one very important truth, namely, that money-of-account is of much greater moment and importance than money in circulation. The pound sterling, though for the greater part of the period unrepresented in the coinage, exercised an influence greater and more permanent than any coin, or even than that of the whole coinage in circulation. The utility of coins is limited to the fleeting transactions of the moment. They are paid, and the transaction ends. But money-of-account endures from day to day, from year to year, and from century to century. All transactions, other than those of an ephemeral character, are conducted by means of money-of-account. All loans, debts, price lists, contracts, mortgages, and indeed all money offers, bargains and transactions not effected immediately on a spot cash basis, have to be conducted in terms of money-of-account and not by means of coin. Even in Tudor England, the volume and value of transactions effected by means of money-of-account exceeded those effected through the circulation of the coinage. As prices rose, as

wealth increased, and particularly as foreign enterprise expanded, money-of-account grew in importance as compared with the coinage. Coins were merely the outward and visible sign of all transactions beyond those concerned with immediate requirements. The inner reality was the record of the money-of-account.

The pound sterling gained its unique prestige and position through being the principal unit of the English money-of-account. Originally it was a mere multiple of the shilling, the value of twenty silver shillings. But it soon established itself as the principal unit of account. For the past four centuries, it has been the most constant, the most important, and the most continuous unit in the English, and subsequently, in the British currency. Whatever changes of value have been effected, either by depreciation of the coinage, by the fluctuations in the relative values of gold and silver, or by paper or metallic inflations, the pound sterling has been the link which connected the old and the new values, and constituted the element of continuity in the monetary system. Past loans, past contracts, past transactions, past liabilities were equated with future payments through the agency of the pound sterling. During the two centuries more immediately under review, a period of fluctuating currencies, rapidly increasing prices, greatly expanding wealth, and an unprecedented acceleration of international commerce, the essential element of continuity in the English currency was provided by the pound sterling.

CHAPTER III

THE BATTLE OF THE STANDARDS

The Guinea

After the restoration of the currency, 1696–98, silver seemed to have established an impregnable position as the permanent standard for British currency. The restoration, so efficiently effected by Sir Isaac Newton, had provided Britain with the finest silver currency in Europe. It was closely allied with the pound sterling, the principal money-of-account, which had established itself as the most permanent and continuous unit in the monetary system. The guinea, soaring away to the fantastic height of thirty shillings in value, did little or nothing to relieve the severe deflation experienced when the old depreciated coinage was being called in, and before the restored currency was issued in any considerable volume. At the commencement of the eighteenth century, there was not the faintest suggestion that the supremacy of silver as the British currency standard was about to be challenged; and that, by the end of the century, its supersession by gold would be an accomplished fact.

There was no direct challenge. The guinea was regarded merely as the last of a long succession of gold coins which flourished for a brief spell and were then discarded. The attack came from an entirely

unexpected quarter. It came in the form of a demand upon the silver currency for which it had not been designed. For the first three-quarters of the eighteenth century silver was called upon to finance the rapidly expanding volume of British overseas investments. The task was performed and the foundations of Britain's remarkable prosperity during the nineteenth century were well and truly laid, but the silver standard perished in the performance of this arduous task. The constant drain of silver from Britain for three-quarters of a century left the silver coinage in such a depleted and depreciated condition that by the year 1774 it was regarded as being incapable of restoration.

Gold did not actually cause the downfall of silver. The guinea simply filled up the blanks in the circulation left by the constant drain on the silver coinage. It was paper money, not gold, which was the monetary cause of silver's downfall. Bank notes were first introduced in Sweden in 1658. They were eagerly accepted in Scotland, but treated with much suspicion at first in England. But in 1694, the Bank of England was authorised to issue bank notes on the security of the interest on the loan to the Government. The issue of these notes came at precisely the time they were most urgently required on account of the deflation caused during the restoration of the currency (1696–98). The timeliness of their issue, and the great convenience they provided, established their popularity. Another kind of paper currency in

the form of Exchequer Bills, carrying interest during their period of circulation, also appeared. So popular were the new forms of paper money that one enthusiastic contemporary wrote, "Parliament laid a good foundation for Paper Money to take the place of silver coins."

But that was not to be the manner in which the supersession of the silver coinage was to be effected. The clue is supplied by the following passages from Cunningham's *Growth of English Industry and Commerce*:—

> During the latter part of the seventeenth century, England was hampered in every way, both as to internal developments and commerce and colonisation, by lack of capital; and the banking system which was inaugurated in 1696 had enormous influence in remedying these evils.

Also:—

> From this time onwards it became a usual thing for careful men to trade upon borrowed capital, since they found they could habitually obtain the loan of it upon easy terms.

The rapid increase of the use of bank notes, exchequer bills and bankers credit greatly stimulated foreign enterprise in the form of colonisation. Outlets were found for the investment of capital in North and Central America and the East and West Indies. But though these enterprises could be financed in their initial stages by paper money and bankers' credit, they had to be paid for ultimately in hard cash. There was at the time no large and expanding export trade, the payments for which could have

financed the foreign investments. The great increase in the British export trade caused by the Industrial Revolution did not take place till towards the end of the eighteenth century; whereas the great increase in foreign investment commenced early in that century.

As there were not enough British exports to finance foreign investments, they had to be financed by cash. Conduitt in his pamphlet, published in 1730, put the matter simply by stating: "When we cannot pay in goods what we owe abroad on account of the Balance of Trade, our debts must be paid in gold or silver, coined or uncoined."

The drain of silver to pay for British investments overseas was a source of anxiety to the Government. Silver was the standard currency, the primary medium of exchange for the country. Gold, on the other hand, was a luxury coinage, a convenience whose loss would not be greatly missed. The reason for the preference for silver for export was, however, clear. The market value of the silver coins was equal, at some periods was above, their coinage value. The market value of the guinea was, on the other hand, much below its circulation value. If a debt of twenty shillings had to be paid in France, it was much cheaper to pay it with silver coinage, worth 20s. in France, than to pay it with a guinea, worth 30s. in England and only 20s. in France. Gresham's Currency Law is to the effect that bad money drives out good money. Any currency circulating above

its market value is, in this sense, bad money, or token money. It will not be accepted at its face value in a foreign country. Only money circulating at its true market value will be accepted in payment by a foreign country. The golden guineas were bad money in this sense; token money, circulating in England above their market value. The silver coinage was good money, acceptable in France at its face value. Hence the constant drain of silver, instead of gold, to France.

In their effort to divert the drain of silver to gold, the Government took active steps to reduce the high artificial value of the guinea. By successive proclamations they reduced the value of the guinea from 30s. to 26s., to 22s., and to 21s. 6d. They did more than issue proclamations. They coined guineas and half-guineas in such numbers that the value of the guineas fell of their own accord to their proclamation value. By 1717, the gold coinage had risen to the figure of over £7,000,000, while the silver coinage had declined to £5,000,000.

So seriously was the drain of silver regarded that Sir Isaac Newton was instructed to prepare a report on "the State of the Gold and Silver Coins of the Kingdom." This report, presented in December 1717, has been described by Jevons as being "the most important document in monetary history." On the practical issue, Newton reported that, while the proclamation value of the guinea in England was 21s. 6d., its market value on the Continent was

between 20s. 5d. and 20s. 8d. He recommended that the guinea should be reduced to 21s. on the ground that the small difference between 21s. and the market value on the Continent was so slight that it would diminish the temptation to export silver. He further recommended that the situation should be carefully watched, so that if the drain of silver continued, a further reduction in the value of the guinea might be made.

The guinea was, accordingly, proclaimed to have the value of 21s., and sufficient guineas were issued to keep it stable at that value. It is important to note that this was the first successful attempt to make a gold coin keep in step with the silver value of the pound sterling. Although the ratio 21 : 20 was an awkward proportion, it was maintained unchanged until the suspension of cash payments by the Bank of England in 1797, that is, for a period of eighty years.

Although the Government succeeded in achieving what had never before been accomplished, that of stabilising a gold coin at a silver value, they failed in their immediate objective. They did not stop the drain of silver. Owing to the generous supplies of gold from the Brazilian mines, the value of the guinea fell to 19s. on the Continent, against 21s., its circulation value in England. However, no action further to reduce the value of the guinea to its market value, as had been suggested by Sir Isaac Newton, was taken.

Sir Isaac retired and was succeeded by Conduitt, whose attitude on the gold and silver question is sufficiently indicated by the following quotations from his pamphlet, issued in 1730: "Gold is as much a measure as silver, and as legal a tender," and "Nine parts in ten, or more, of all payments in England are now made in gold." Conduitt, as Master of the Mint, found it much more profitable to swim with the stream, to buy gold on the Continent for 19s., and coin it into English guineas at 21s., than to try to stem the flow of silver from England to India and to the Continent.

Conduitt's policy diverged widely from that of Sir Isaac Newton. Sir Isaac was a strong supporter of the silver standard, and, subsequent to his report in 1717, he stated that "silver remained, according to the fundamental laws of the realm, the sole true money." Conduitt's policy, which was accepted by the Government, may be expressed in the phrase—"let the best metal win." He enunciated the principle that the standard or measure of currency was the value of an ounce of silver, but he perceived that its application was rather with reference to foreign trade than to the internal circulation. He was not afraid of Gresham's Law, nor of the fact that, according to that law, the guinea, circulating above its true market value in England, was bad money. It might be bad money in the sense that it could not finance foreign trade, but it was perfectly good money for the internal requirements of England.

The effect of this policy was to substitute gold for silver as the principal currency in England. Silver was allowed to drain away, and as it went guineas and half-guineas were coined in profusion. The numbers issued were such as to maintain the internal value of the guinea at the constant value of 21s., both with respect to the silver coinage, and to the money-of-account, the pound sterling. The silver coinage was reduced to a deplorable condition of scarcity and depreciation. It was naturally the full-weight coins which were exported. Light-weight coins would have been received in France at their depreciated value. Consequently they remained behind, while all the good silver money disappeared.

As the gold coinage increased in popularity, the silver coinage went from bad to worse. The silver crowns and half-crowns had completely disappeared by 1760, and in 1774 the silver coinage was so debased that it was limited as legal tender to the sum of £25. This was the first legal acknowledgment of what had for some years been an accepted fact, that gold had virtually superseded silver as the standard currency of the country. The gold coinage had risen in volume to over £20,000,000. The silver coinage had shrunk to less than £2,000,000, and was represented by coins so worn and debased that they had lost a large proportion of their value.

From 1774 till 1797, when cash payments by the Bank of England were suspended, England was virtually on a gold standard. Hawtrey, writing of

this period, in his *Gold Standard in Theory and Practice*, states: "The virtual Gold Standard to which the public had become accustomed, was founded on nothing but the over-valuation of gold in the coinage system." The guinea had circulated for over a century at a value much above its market value. It was, in that respect, a token money. It was useless for financing foreign trade. According to Gresham's Law it was bad money. But, according to the internal requirements of Britain, it was perfectly good money. It had a quality of stability of value which the silver coinage had never possessed. It had linked itself at a constant ratio with the money-of-account, the pound sterling, a feat which no previous gold coin had ever succeeded in achieving. By its practical success, contrary to the doctrines of orthodoxy, it had afforded valuable lessons in currency management, which proved to be of great value when the future currency policy of Britain had to be determined.

The Battle of the Standards lasted roughly for three-quarters of a century (1700–74). The contest had three well-defined phases. During the first phase (1700–17) the Government made persistent efforts to defend the silver coinage from the constant drain of silver due to the necessity of financing overseas investments. During the second phase (1718–30) the Government relaxed the efforts previously made to defend the silver coinage from being exported, and was content to counteract the growing deficiency of the silver coinage by a generous issue of guineas and

half-guineas. During the third phase (1731–74) the gold coinage continuously improved its advantage while silver progressively declined until it was no longer fit to be the standard currency of the realm.

By a stroke of irony, the cause which had produced the drain of silver from the country ceased just about the time when silver was disestablished from its position as the standard currency. The Industrial Revolution commenced to make itself felt about 1770. It needed much capital for its development, and the current of investment overseas was diverted for a time to investment in home industries. The rising exports produced by the increasing home industries were more than sufficient to pay for the decreased amount of overseas investment. Silver was no longer required for export. It began to appear at the Mint, voluntarily, for coinage, a phenomenon unknown since the beginning of the century. But the relief came too late. Silver was hopelessly discredited as a coinage. Gold was far too firmly established for silver to be restored. The silver seeking coinage did nothing more than help in a very small way to remedy the defects and deficiencies of the existing silver currency.

A blow of even more cruel irony was struck at the guinea in its hour of triumph. The French Revolution, followed by the Napoleonic wars, raised the price of gold on the Continent, and transformed the guinea from a coin circulating in England above its market value into a coin with a market value of more than

21s. Under Gresham's Law the guinea became "good money." From that moment its doom was sealed. The test of "good money," according to Gresham's Law, is its capacity to disappear in critical times. The guinea passed the test by disappearing rapidly to the Continent. The gold coinage, which had reached the high level of £25,000,000 in 1790, disappeared so rapidly that in 1797 the Bank of England was forced to suspend cash payments.

For the next eighteen years, Britain's currency was on neither a silver standard nor a gold standard, but on an inconvertible paper standard, exactly the same standard on which the British currency, after the departure from the gold standard in 1931, was based. The paper interregnum was fatal to the revival of the guinea as a coin. The guinea was killed by its supreme virtue, its stability. For eighty years, from 1717 to 1797, the guinea had proved that by a judicious exercise of currency management, it was possible to establish a gold coin which would maintain a constant ratio with the silver coinage and with the money-of-account, the pound sterling. True, the ratio established, 21 to 20, was most inconvenient. But that could be easily corrected. The great service which the guinea had rendered to the British currency was that it pointed the way to stability. Its predecessors, the sovereign, the gold pound, the unit, the broad, had all failed in this essential quality. The guinea itself during the first fifty-five years of its existence (from 1662 to 1717) had followed their bad example. But

for the last eighty years it had demonstrated by actual experience, amid wild currency fluctuations in other directions, that currency stability was an attainable goal.

When the time came for the resumption of cash payments, the lessons learnt from the experience of the circulation of the guinea were invaluable. But as compared with the pound sterling of 20s., the guinea at 21s. was hopelessly out of the running as a candidate for adoption as the new currency unit. The new unit was to combine the tradition, the prestige, the continuity of the pound sterling with the stability of the guinea. The guinea as a coin was dead. But it still lives a respectable shadowy existence, as a courtly M.C., conferring pride of place in subscription lists, to all who are willing to pay an extra shilling in the pound for the privilege.

CHAPTER IV

THE STERLING STANDARD

An International Currency

THE suspension of cash payments in 1797 provided a unique opportunity for a complete reconstruction of the British currency system. By 1816 the break with the past was so complete that the requirements of the future could be considered without any embarrassing regard for the claims of the past. Everything that had proved valuable in the past could be retained; anything that had proved unserviceable could be discarded.

The first thing to be done was to survey the currency as it actually was in 1797 before cash payments were suspended. Of the silver currency only a scanty and discredited remnant remained. The silver standard had disappeared, and there were no valid grounds for its revival. It was indeed a false standard, the value of an ounce of silver. But the value of an ounce of silver was not a standard at all. It was a fluctuating standard of value, and the essential quality of a standard is that it should be a fixed unit of the thing to be measured. Conduitt had placed on record that the silver standard, the market value of an ounce of silver, had changed with reference to its currency value as many as seven times in five years (1713–18) at a time when silver was pre-eminently the standard of currency.

By analogy with the physical sciences, a standard of currency must be a fixed and stable unit of value. A standard which fluctuated through seven changes of value in five years was utterly unsuitable to be a currency standard. The old silver standard was accordingly dismissed from consideration.

There were many objections, too, to the adoption of a revised scientific standard based on a fixed silver value. The market value of silver fluctuated much more violently than that of gold. There were grave doubts whether, even if a fixed value of silver should be established for currency purposes, the currency authorities would be able to keep the market value fixed at the currency value. All experience was against the possibility of maintaining the market price of silver at a fixed figure for any length of time.

Another objection was the difficulty of the selection of a silver coin in which to embody the fixed value of silver. The new standard must be closely associated with the pound sterling, the principal monetary unit-of-account. A silver coin of that value was out of the question. The shilling was too low in value to form a convenient currency standard, suited to the large financial transactions of the nineteenth century. The crown was not a convenient value for account purposes. Moreover, the crown had vanished from circulation over fifty years ago. The silver currency was hopelessly discredited. No one living in 1816 had had any experience of an efficient silver currency in

England. Since 1730 it had progressively deteriorated, and it had become a byword for inefficiency.

Gold was obviously the metal to be used as the basis of the new scientific unit of currency. In the form of the guinea it had already provided a coin which had remained stable with the silver coinage and with the unit-of-account, the pound sterling, for eighty years. The guinea was undoubtedly an inconvenient value to be adopted for the unit. But the guinea had originally been designed to circulate at 20s. Sir Isaac Newton, in 1717, had contemplated a further reduction of the guinea below 21s., and it is highly probable that had his policy been adopted in full, the guinea would have been stabilised at 20s. in 1718.

The final decision was to the effect that the old-established unit-of-account, the pound sterling, was to be made the unit-of-value, or standard, of the new currency. The pound sterling, which had been valued at twenty silver shillings for nearly three centuries (1489–1774) had also been associated in value with the guinea for twenty-three years, from 1774 to 1797, during the period when silver was virtually de-standardised. It then kept an independent value, based on the value of the £1 notes in circulation, for a period of nineteen years, during the period of the suspension of cash payments. It was now to be made a definite standard of value, based on the mint value of gold at which the guinea and the pound sterling had been associated from 1774 to 1797.

The new standard was an excellent blend of all that was useful from the old system, with all that was necessary to meet the requirements of a new century. It was both conservative and revolutionary. It was conservative in preserving the continuity of the pound sterling. It was conservative in preserving and maintaining the stability of the gold currency which had been established by the guinea for a period of eighty years' duration. It was conservative in restoring the guinea to its original value of 20s. It was conservative in carrying out Sir Isaac Newton's expressed policy of a century previously that a further reduction in the value of the guinea might be made. It was conservative in adopting as its fixed value of gold for the new unit of value, the mint price of gold £3 17s. 10½d. per ounce, which had formed the connecting link between the guinea and the pound sterling prior to the suspension of cash payments.

But the revolutionary elements of the new currency far exceeded those of a conservative nature. Silver was finally abandoned as a standard both for the money-of-account and for the coinage. The pound sterling was transformed from its traditional value of twenty silver shillings into a gold value based on the mint price of gold, £3 17s. 10½d. per ounce. The guinea was abolished. A new coin, called by the revived name of the sovereign, was to represent the new unit of value, the pound sterling, in currency. The coinage was equated to the money-of-account through the equivalent gold values of the sovereign and the pound sterling.

The possibility of a double standard was eliminated by limiting to £2 the legal tender of payments in silver.

The most revolutionary change of all was the substitution of a unit of value instead of a weight of silver as the new currency standard. The new standard was not gold, nor a weight of gold, but a value of gold. The value of gold selected for the standard could be expressed in two ways. It could be expressed either in the form that an ounce of gold was valued at £3 17s. 10½d.; or in the form that the value of 5 pennyweights 3·274 grains of gold was worth one pound sterling. Both expressions meant the same fixed valuation of gold, which was adopted as the new standard of currency.

The new standard was given the name of "the gold standard" in contradistinction to "the silver standard" which had previously been the traditional standard of currency. But the designation "the gold standard" for the new currency was incorrect. It suggested that the change effected in 1816 was merely a transfer from silver to gold. That is not correct. The change then effected was a much more revolutionary change than a mere change of metal. It was a change in the scientific basis of the standard. It was a change from a false to a true standard. It was a change from a unit of weight to a unit of value. It was a change from an unstable fluctuating value of silver to a fixed stable value of gold. The distinctive element of the new standard was not its gold but its stability. The

new standard was, in brief, not "the gold standard," but the fixed value of gold adopted as the standard, the pound sterling value of gold, the sterling standard.

Having adopted the sterling value of gold, £3 17s. 10½d. per ounce, as the standard of currency, it was necessary to take measures to ensure that gold should return to this value, and thereafter be fixed at this value so securely that it would be independent of the disturbing operations of supply and demand. In 1816 gold was over £4 per ounce, and the first measure to take was to resume cash payments until the value of gold fell to the sterling level adopted as the future currency standard. This course was taken gradually, and it was not till six years subsequently, in 1822, that the Bank of England was able to make full payments in gold of all notes presented for encashment. The resumption of cash payments removed the discount at which the bank notes had previously circulated, and gold began to circulate at its sterling value.

Further measures were necessary to ensure that gold should not in future depart from its sterling value. To ensure this objective, it was prescribed that the import and export of gold to and from Britain should be free; that the Bank of England should be required to purchase all gold on offer in unlimited quantities at £3 17s. 9d. per ounce, and to sell all gold on demand in unlimited quantities at £3 17s. 10½d. per ounce. These measures linked the value of gold to

the pound sterling, and linked the pound sterling to the value of gold in such a manner that they could not diverge beyond the limits fixed. The narrow margin between the buying and selling price, a margin of 1½d. only, gave a slight degree of play, less than two points in a thousand, and prevented the connection from becoming stiff with rigidity.

In the popular mind, the return to the gold standard was associated with the circulation of sovereigns and half-sovereigns after the resumption of cash payments in 1821. This was but a superficial aspect of the revolutionary change which had been effected. The circulation of sovereigns and half-sovereigns was not, in principle, different from the circulation of guineas and half-guineas during the preceding century, from 1730 to 1797. It was a mere matter of internal currency, whereas the efficacy of a currency standard depends on its international behaviour. It was the external drain of silver which had been responsible for the breakdown of the silver standard. The test whether the new gold standard would stand the strain of financing overseas commerce and investment would determine whether it would be a success.

The measures taken fixed the value of gold throughout the world. While Britain continued to be a free buyer and a free seller of gold at a fixed price, no other value of gold was possible. If gold tended to rise above the Bank of England price, it could be purchased in unlimited quantities at the Bank, and a profit secured. On the other hand, if gold tended to fall below that

price, it could be sold to the Bank of England also at a profit.

What made the currency revolution of 1816 unique was that, for the first time in the history of the world, there was a fixed and stable value of gold and of currency, which operated, not temporarily nor locally, but permanently and throughout the world. Britain had provided the world with a new currency factor, a fixed unit of value.

As soon as the world grasped this fact it hastened to take advantage of it. The stability of currency established by making the pound sterling a fixed value of gold was not confined to Britain. It was extended to the whole world by means of the Sterling Bill of Exchange. Bills of exchange had been used to finance international commerce from time immemorial. But never before had bills of exchange, as good as gold, been available in unlimited quantities to every trader in the world, from China to Peru, on application to his local banker. As good as gold! The Sterling Bill of Exchange was better than any gold of which the world had previously had any experience. The Sterling Bill of Exchange was encashable in a new kind of gold, a gold with a fixed stable value, instead of in the old unstable fluctuating gold, whose value was just as likely to go down, as up, while the bill was current.

The revolution in international currency effected by the establishment of the sterling standard by Britain was much greater, and had much more far-

reaching consequences, than the revolution effected in the internal currency system. The Sterling Bill of Exchange provided for the merchants of every country in the world a reliable, stable, efficient international currency. They accepted the unexpected gift with alacrity. The eighteenth century had witnessed a grim, prolonged struggle between Paris, London, and Amsterdam as to which should be the financial centre of the world. With the sterling standard, Paris and Amsterdam faded out. London alone remained, indisputably, unquestionably the financial centre of the world, with the Bill of Exchange on London establishing its predominance as the most efficient international currency the world had ever known, available for every country and every commercial centre.

The enormous expansion of international commerce, witnessed throughout the world during the nineteenth century, was founded on the Sterling Standard and the Sterling Bill of Exchange. The commercial dominance of Britain is usually attributed to the Industrial Revolution which transformed Britain into the foremost manufacturing country in the seventy years elapsing between 1770 and 1840. But the Industrial Revolution could not have produced its effect if it had not been supplemented by an efficient system of international currency, enabling its products to be distributed with unprecedented economy to all the countries of the world. That efficient system of currency was provided by the sterling standard, in its inter-

national form, the Sterling Bill of Exchange. The sterling standard was, indeed, one of the most potent influences in the rapid development of the world during the nineteenth century.

CHAPTER V

THE INTERNATIONAL STANDARD

The Drain of Gold

A BILL OF EXCHANGE is a post-dated cheque. It is post-dated with the consent of both parties to the transaction. Its purpose is to secure the financing of the value of goods in transit from one country to another. The exporter wishes to receive payment as soon as the goods are shipped to their destination. The importer does not wish to pay until the goods are delivered into his charge. This disparity of time is bridged over by the bill of exchange, which transfers the responsibility of financing the value of the goods during the period of transit to a bank or to a financial house which makes a speciality of such transactions.

An exporter is paid for his goods exported by a bill of exchange, payable at some future date, usually three months ahead. Upon shipment he takes the bill of exchange, together with the bill of lading for the goods shipped, to his banker, who pays him the amount of the bill, less a small discount. The bill is then forwarded to a bank or discount house at the Money Market on which the bill is drawn. There it is accepted by the agent of the importer, acceptance being an undertaking to pay the amount of the bill in gold on the due date. It is kept till the date fixed for payment, and then settled.

The great advantage of the Sterling Bill of Exchange was that it was payable in gold, and that the sterling standard had given gold a fixed value throughout the world. No bill of exchange, drawn in any other currency, provided this advantage. Other subsidiary advantages were secured to its patrons by the fact that the London Money Market provided unrivalled facilities for all transactions connected with the Sterling Bill of Exchange, whether discounting, re-discounting, acceptance or settlement. No other bill of exchange provided such qualities of certainty, stability, and facility of payment.

Owing to these advantages, the Sterling Bill of Exchange was used to finance not only goods in transit to and from Britain, but also goods in transit to and from all countries. The cargoes of ships exported from one foreign country to another, even though neither ships nor cargoes came within a thousand miles of any British port, were usually financed by Sterling Bills of Exchange, rather than by bills drawn in the currencies of the exporting or importing countries. Between 80 and 90 per cent of all cargoes on the high seas were so financed. This meant that the London Money Market was bearing the cost of financing the value of nearly nine-tenths of the overseas commerce of the world.

The method of settling the payment of the bills of exchange between the various countries, as they fell due, was somewhat analogous to that of settling a bridge score. The payment due to an exporter operated

as a plus to the country of export, and as a minus of the same amount to the debit of the country importing. The number of bills becoming due on any given date was at first comparatively small. But gradually the numbers grew, and as they became larger the possibilities of balancing the minuses against the pluses, in the international game of bridge played with the bills of exchange falling due on the London Money Market, became greater. The larger the total number of bills falling due, the greater was the number of cancellations against each other. At the close, there were left the inevitable residue of pluses and minuses, creditable to, or debitable to, the various countries, which could not be cancelled out and had to be settled in gold. But these payments in gold were small in comparison with the total number of transactions settled. As the system grew, and the number of bills of exchange for settlement reached large dimensions, the proportion of gold payments from country to country to the volume of the total transactions settled, became less and less.

Stimulated by this most efficient method of financing international transactions, world development proceeded at a more rapid pace than ever known previously. But one grave danger threatened. Some countries appeared to have exceptional luck in the international game of the settlement of the exchanges. A few countries seemed to get all the pluses. The remaining countries were usually debited with minuses. There were four countries, Britain, France, Holland,

and Belgium, which nearly always came out on the right side, leaving the remaining countries in the unfortunate position of having to pay up in gold. These four countries were the creditor countries. In the past they had invested large sums in developing the debtor countries, and the repayment of the sums invested, or the payment of interest on the sums invested, appeared in the exchanges, and influenced the final balances in the manner described.

The final plus balance due to Britain was by far the greatest of the four. The great drain of silver during the first part of the eighteenth century, and subsequently the great volume of exports produced as the Industrial Revolution proceeded, had given Britain a strong position as a creditor country, with investments spread over most of the countries of the world. This creditor position was strongly reinforced by payments for services, such as shipping, insurance, and banking, which Britain was providing for the rest of the world. The creditor positions of France, Holland, and Belgium were far smaller than those of Britain; and besides, France, Holland, and Belgium were still on a silver standard. It was possible for the debtor countries to commute the final balance of their gold indebtedness to these countries by silver payments at the current rate of exchange.

But this relief was not possible in the settlement of the final gold balance due to Britain. Britain was on the sterling standard, a gold standard, which required that these balances must be paid in gold. The

payment of the large gold balances due to Britain on account of her strong creditor position created a strong flow of gold from the debtor countries to Britain. The drain of gold from the debtor countries gradually grew to be a menace to the rapidly expanding international commerce which had been so strongly stimulated by the international operation of the sterling standard.

At first this movement of gold to Britain was welcomed as strengthening the internal financial position of the country. Gold was required in large quantities for the resumption of cash payments by the Bank of England; then for the creation of adequate reserves for the internal note issue; and, finally, for the provision of gold reserves for the enormous international commitments, which were being undertaken by the London Money Market, now that London was the financial centre of the world.

A few figures may be cited to indicate the volume of gold required to place Britain on a sound footing for operating the sterling standard. In 1816 there were £60 millions of bank and country notes in circulation, supported by only £7 millions of gold reserves in the Bank of England. By 1822 gold coins to the extent of £17 millions had been put into circulation and the gold reserves at the bank had been increased to £10 millions. The resumption of cash payments had necessitated the import of £20 millions of gold, in the five years 1817–22. This amount was required for the purposes of internal circulation only. An equal

amount in addition was required in order that the London Money Market should be in a position to make cash payments on demand with respect to the immense international liabilities it was incurring.

Necessary as this drain of gold was for the purpose of establishing the sterling standard, great as were the benefits to the commerce of the world resulting from the establishment of the sterling standard, the loss of gold was deeply resented by the debtor countries. The extent of the drain, and the feelings of resentment it engendered in the debtor countries, are expressed in the following two passages from *Silver and Gold*, a standard work by the eminent American statesman and financier, Samuel Dana Horton:—

> But under the Act of 1816, the currents of Gold and Silver, which before the war could flow in and out of Great Britain indifferently were henceforth enclosed in dykes and locks. Gold flowed in from the Continent, as we have seen, and bared it of its share of its International Money, but could not flow out in response to some special demand from abroad.

Also:—

> The lake of silver and the lake of gold were joined together only by the narrow and tortuous channels of exchange—shallow channels too, for the great mass of silver on the Continent, and gold in England, under the laws of legal tender, must remain in position below the ordinary tides of change.

The inevitability of a drain of gold from debtor nations to protectionist creditor countries under a gold standard was carefully explained in the Report

of the Macmillan Commission, issued in 1931. The explanation was made with special reference to the recent drain of gold to France and the United States; but as it applies with equal relevance to the drain of gold to Britain a century ago, it serves to explain clearly why it occurred, and also the measures then taken by Britain to relieve the dangerous situation that developed. Britain was, of course, a strongly protectionist country during the early portion of the nineteenth century. The relevant paragraphs in the Macmillan Report dealing with this problem are numbers 184 and 310 to 313. These are too long to quote, but the following paraphrase pieced together from these paragraphs, with the minimum of modification to make them read connectedly, gives their substance:—

> Creditor countries must, unless they are ready to upset the economic conditions, first of the debtor countries and then of themselves, be prepared to lend back their surplus, instead of taking it in gold. The first measure towards the restoration of the international price level must necessarily be taken on the initiative of the creditor countries. It must consist, partly, in a greater willingness to buy, and partly in a greater willingness to lend. Failing this the creditor countries will soon have sucked in all the gold available in the hands of the debtor countries, and this may entail a series of defaults. It is unlikely therefore that the debtor countries can continue much longer to square their international position by parting with gold at the rate of £70 millions a year, as they have been forced to do in the last two years. These figures emphasise the impossibility of the debtor countries as a whole meeting their obligations otherwise than out of new loans or by selling more goods at better

prices. For the creditor countries to fail in taking steps to relieve this stringency would be exceedingly short-sighted, having regard to their own creditor position.

No words could be graver than these solemn warnings. They describe a desperate financial position on the brink of disaster. They indicate clearly the immediate steps necessary in 1931 to rescue the world from its perilous position. But they fell on deaf ears. France and the United States still continued in a policy which would have brought the world and themselves to ruin if Britain had not intervened in September 1931, and on her own initiative reversed the progress towards disaster.

Returning to the early days of the operation of the sterling standard, it was fortunate that Britain had, in 1831, a clearer knowledge and a more accurate conception of international finance and commerce than was possessed by France and the United States a century later in 1931. Britain did not in the early days of the sterling standard require a Royal Commission to tell her that if she ruined her customers she would lose their trade, and that if she drained away from her debtors their means of payment they would default. These were elementary axioms of trade, known in every huckster's shop in the country. It did not need much imagination to appreciate that they applied equally to international trade. As soon as it was understood that the operation of the sterling standard was causing serious embarrassment to Britain's customers, steps were taken to remove the defects in its working.

These could be ascertained by studying the working of the new international currency, the Sterling Bill of Exchange. This had proved a magnificent trading asset, a currency capable of indefinite expansion, and yet immune from the dangers of inflation. Each bill of exchange had its counterpart in the goods in transit to their destination; and each bill of exchange ceased to be current when the goods it represented were distributed. There could be no inflation because the total of this class of currency was always exactly equal to the total value of the goods it financed.

But it had its limitations. It was not a one-way currency. It could not be used entirely for selling. It could only function efficiently if it were used for both buying and selling in approximately equal volumes. It was a currency which depended on the principle of balance for its efficacy. The merchants of London soon discovered this principle of mutuality inherent in the working of the bill of exchange. The customers anxious to purchase British goods wished to pay for them in the new international currency, bills of exchange, and not with gold. But the only method of obtaining bills of exchange by which to purchase British goods was by first selling their produce to Britain. That was the only way in which they could continue to remain as purchasers of British goods. They must first obtain the necessary international currency, bills of exchange, by sales to Britain.

The merchants of London in this manner discovered that it was not alone the sterling standard

which was causing the drain of gold and ruining their customers. It was Protection. That was the enemy. It was robbing the Sterling Bill of Exchange of half of its efficacy by forcing it to operate as a one-way currency. It was defeating British export trade by keeping foreign customers short of the international currency, bills of exchange, with which to buy British goods.

There is an extremely foolish fiction, very popular with certain sections of the Press, that Free Trade was forced upon a reluctant Britain by the agitation of Cobden and Bright. As a matter of history, the British movement towards Free Trade was started by the merchants of London nineteen years before the Cobden–Bright agitation and the foundation of the Anti-Corn Law League. Britain had adopted Free Trade before the agitation of Cobden and Bright had commenced. Their agitation was directed against the one outstanding relic of Protection, the Corn Laws, when the principles of Free Trade in all other directions had already been adopted.

The movement towards Free Trade was commenced by a very influential petition from the merchants of London to the House of Commons in 1820 asking for the removal of the restrictions imposed on free commercial intercourse. The Committee of the House to which the petition was referred expressed general agreement with the objects of the petition. So strong was the movement that in 1824–25 very considerable reductions and modifications of the tariffs previously

imposed were effected. This was only the beginning. Once started, the movement gathered force. Between 1832 and 1839 Customs and Excise Duties, to the extent of over £3,000,000, were remitted. The formation of the Anti-Corn Law League in 1839 hastened a movement which had already acquired a great momentum, and brought it to a complete triumph in 1846.

The Free Trade movement followed closely after and was undoubtedly inspired by the establishment of the sterling standard in 1816. As the Macmillan Report demonstrated a century later, Protection is an impossible policy for a creditor country on a gold standard to pursue. This truth was discovered and acted upon by Britain in the eighteen-twenties. Either the sterling standard or Protection had to go. The former was retained, the latter discarded.

This operation of the sterling standard furnishes an explanation of what has hitherto been regarded as an unexplainable paradox, the fact that other countries refused to follow the example of Britain and adopt Free Trade. Britain was the only country to adopt Free Trade, because Britain was the only country forced by the inexorable pressure of international commerce to take that action. With the adoption of the gold standard, Britain found herself in the possession of an extremely powerful weapon to enforce the payment of any liabilities due to her in gold. It was a weapon much more potent than any form of legal distraint. It worked automatically and it

worked unconsciously. It was not until it had been in operation for some years that its potency and the nature of its action were appreciated. Indeed, it was not until the Macmillan Report was issued in 1931 that it was fully realised that a protectionist creditor country on a gold standard is a dangerous menace to the world, and ultimately to its own prosperity.

In the early days of the sterling standard, Britain realised, but perhaps not so clearly as it is now appreciated, that she was in possession of this enormous power for good or evil. A narrow, nationalistic administration of the new currency system would have speedily brought the world to disaster. The comparatively small volume of monetary gold then in circulation would soon have been drained into the vaults of the Bank of England, and a crisis similar to that which developed in 1931 would have developed a century earlier. But the international interests of Britain precluded the adoption of so narrow and restricted an administration of the new international currency. British exports were dependent on the solvency and the prosperity of the rest of the world, and rendered world prosperity of paramount interest to Britain. Free Trade was adopted because it mitigated the rigours of the debt-collecting potency of the gold standard. It gave Britain's debtors the option of paying their liabilities in goods, an option of which they gratefully availed themselves.

Other countries were free from these considerations

rendering the adoption of Free Trade imperative for Britain. It is not necessary to assume that Britain was altruistic or philanthropic in her adhesion to Free Trade. It happened that the interests of Britain, as the supreme creditor nation of the world, and as the originator and administrator of the international currency, were identical with those of the rest of the world. Other nations, not so dependent on or interested in the general prosperity of the world, were free to pursue their own interests in a more purely national direction. Not being compelled in their own interests to adopt Free Trade, they refrained from following Britain's example.

With the gradual adoption of Free Trade by Britain, the nature of the settlements of the matured bills of exchange on the London Money Market gradually changed. The Sterling Bill of Exchange, freed from the incubus of Protection, was able to function naturally as a two-way currency. It had no longer to waste more than half its energy in acting as a suction pump to drain gold from reluctant countries which were placing every obstacle in the way of its departure. Its operations became more balanced, more efficient, more at the service of commerce and world development. Being able to sell their produce in the free market of Britain, the newly developing countries obtained in exchange the necessary currency in the form of bills of exchange, which enabled them to pay for their own requirements without having to part with their gold. Their minuses disappeared from the settlements

on the London Money Market, and Britain's enormous, unwanted, and embarrassing plus also disappeared.

The very greatly increased currency resources of the newly developing countries made them far better customers for British produce. The sterling standard had given an international currency to the world, but it was Free Trade which distributed this currency in the form of bills of exchange freely to every nation able to market its produce in Britain. The magnificent progress of international commerce during the nineteenth century was based on the operation of two complementary factors, both British in their inception, the sterling standard and British Free Trade.

The combined effect of the sterling standard and Free Trade was a great diminution of the importance of gold in financing international trade. The Sterling Bill of Exchange had largely superseded gold as an international currency, gold being required only to settle the small balances remaining after the bills of exchange had been set off against each other. Free Trade had reduced these balances requiring settlement by gold payments to even smaller dimensions. The nations of the world reposed their confidence in the Sterling Bill of Exchange, not because it was ultimately payable in gold, but because they knew that the London Money Market would so balance the bills against each other that international payments of gold would be reduced to infinitesimal quantities in proportion to the total volume of transactions. The

sterling standard, combined with Free Trade, had gone far to eliminate gold as the dominating factor in international commerce. Gold had been reduced to its true position, as the servant, and not the master, in the world of trade and industry.

CHAPTER VI

THE MANAGED STANDARD

The Bank Rate

THE history of currency since 1816 has been distorted by two "bankers' fictions." The first is the fiction that there is such a currency standard as "the gold standard." The fallacy that the various international currency standards, which have operated since 1816, are one and the same standard, which can be conveniently described as the gold standard, not only brings confusion to students and investigators; it has brought nations to the brink of disaster.

But there is a companion fiction, just as misleading, though not nearly so disastrous in its results. It is the fiction that this so-called gold standard was automatic in its working. The fiction was thoroughly exposed by the Macmillan Report. It now lives only in controversial articles, in which all proposals for currency reform are contemptuously branded with such terms as "managed currencies" and "currency manipulation." It does not seem to occur to the users of such phrases that the various gold standards which have operated since 1816 have been in every sense of the term "managed currencies," and that any success they have achieved has been due to the wisdom and experience devoted to their "manipulation."

The Macmillan Report dismisses the claim that a

gold standard can be automatic in its operation by stating that "the sense in which the gold standard can be said to be automatic is thus very limited; it is automatic only as an indicator of the need for action, and the end to be achieved." The importance of management in any system of currency is demonstrated by the fact that two sections of the conclusions of the Report as to the "Main Objectives of the Monetary System" are headed "International Currency Management" and "Domestic Currency Management." As to the intricate nature of the management required, the Report lays down that "the management of an international standard is an art, and not a science; and no one would suggest that it is possible to draw up a formal code of action."

In order that in future there shall be no doubt on the subject, the Macmillan Report uses the following emphatic language:—

> The monetary system of this country must be a Managed System. It is not advisable, or indeed practicable, to regard our monetary system as an automatic system, grinding out the right result by the operation of natural forces aided by a few maxims of general application, and some well-worn rules of thumb.

So remarkable has been the change of opinion in this respect in recent years that even the eminent American opponent of managed currencies, and the staunch supporter of the gold standard, Professor Kemmerer, now states: "The public should not be unduly scared by the term 'managed currency,' all currencies have in recent years been more or less

managed, even the gold standard currencies themselves."

From its inception the sterling standard depended for its very existence on a superlative exercise of the art of management. The sterling value of gold, £3 17s. 10½d. per ounce, is not (as can be verified by a glance at the papers any day) the natural value of gold. It was an artificial value, selected for very good reasons to be the basis of working the sterling standard. But it did not remain automatically at that value. It could only be kept at that value by the exercise of superb judgment and management. That the Bank of England was able to maintain the stability of the value of gold at this artificial figure for ninety-two years in a world of rapid progress and development against numerous pulls both of supply and demand, was a remarkable feat of management that even now is not appreciated at its full value.

The drain of gold from the debtor countries to Britain demonstrated quite early in its career that the sterling standard could not be permitted to work automatically. It was producing such dislocation in the world by its automatic operation that it was impossible to restore equilibrium by purely financial methods. It was necessary to have recourse to the political world, and to revise the traditional tariff-policy of Britain, in order to enable the sterling standard to work satisfactorily. Judged from a purely currency point of view, the adoption of Free Trade by Britain was a piece of supremely successful cur-

rency management. It demonstrated that the currency revolution effected in 1816, though it caused an immeasurable improvement over the confusion which had previously existed, still required very careful supervision and management, if it was to produce the best results in the course of its operation.

One recommendation from the Macmillan Report, which has previously been quoted, is to the effect that creditor countries should show "a greater willingness to buy" from the debtor countries and "a greater willingness to lend" to them. By the adoption of Free Trade, Britain had showed a greater willingness to buy. Was it possible by any system of guidance or management to induce Britain to show a greater willingness to lend?

A reference back to Chapter III will show that in the eighteenth century there was no need to induce Britain to show "a greater willingness to lend." Britain lent to other countries to such an extent that she used up the coinage of her standard currency to finance her overseas investments. But with the Industrial Revolution, a large proportion of investment was diverted from foreign to home enterprise. The Industrial Revolution (usually dated 1770–1840) was still in progress when the sterling standard was established and Free Trade adopted. In particular, large sums were being invested in home railway enterprise between 1830 and 1840. For these reasons Britain's willingness to lend to the debtor countries was restrained by large investments at home.

The Bank of England had found by experience that a very potent weapon in keeping the value of gold constant at its sterling value between the limits of £3 17s. 9d. and £3 17s. 10½d. per ounce was the manipulation of the Bank Rate. By judiciously raising or lowering the Bank Rate, the Bank of England could counteract any tendencies of the value of gold to escape from confinement between these narrow limits. There was at first no consciousness that this action also stimulated and retarded overseas investments. But, by the lowering of the Bank Rate, investment at home would have to be made on less favourable terms, and investment overseas would be accordingly stimulated. On the other hand, the raising of the Bank Rate retarded investment overseas and stimulated it at home. Experience soon made the Bank of England conscious of the control over investment conferred by the power to modify the Bank Rate. It was also perceived that this control over investment gave to Britain complete control over the Balance of International Trade.

In 1730 Conduitt had drawn attention to the fact that the Balance of Trade had to be settled by the payment of gold or silver, coined or uncoined. This necessity of effecting a settlement of the Balance of Trade had caused a prolonged drain of silver from Britain in the eighteenth century, and an embarrassing drain of gold to Britain on the establishment of the sterling standard. Free Trade had stopped the drain of gold, and created a rough and ready Balance of Trade by establishing a two-way international currency and

facilitating the cancellation of bills of exchange against each other. This meant that the Balance of Trade was being adjusted by goods rather than by gold. Bills of exchange were simply the financial expression of the goods in transport from country to country. In so far as the bills of exchange balanced, gold was being economised, and the exchanges of goods were balancing themselves independently of gold. The manipulation of the Bank Rate provided a supplementary and a much more delicate means of adjusting the Balance of Trade. While the operation of Free Trade brought the residual balancing payments of gold to small dimensions, it was possible by the supplementary action of the Bank Rate to abolish them altogether.

In a previous chapter Dr. Miller, the American financier, has been quoted as defining the gold standard as "a set of practices, a system of procedure, never formulated, never consciously thought out." With the discovery by the Bank of England that it could control movements of capital by the operation of the Bank Rate, its policy "never formulated" was to abolish the active use of gold in the settlement of the International Balance of Trade. With the powerful and skilled assistance of the London Money Market, short loans were utilised to settle any slight differences that appeared at the close of each day's settlement. These adjusted themselves in due course unless there happened to be a definite and prolonged movement one way or the other. If such a movement was sufficiently pronounced to threaten to transfer gold from one

country to another, then the Bank Rate was utilised to correct the tendency. Gold movements declined till they represented little more than the distribution of the newly mined gold to the countries most in need of it.

For over half a century Britain remained in sole and supreme control over the international currency she had invented and given to the world. In 1872 Germany, assisted by the war indemnity she had extracted from France, joined the sterling standard. The fact that the incorrect description of "the gold standard" was applied to the system, somewhat disguised the extremely British character of its management and control. The two fictions—the name "the gold standard" and the belief that it was automatic in its working—were sufficient to induce Germany to join what it believed to be a completely automatic international system. The facts that the system was international in its operation, and that its supervision and control by Britain were achieved with such apparently effortless ease, disguised the fact that Germany had joined a British system of international currency based on the sterling standard, under cover of the neutral name "the gold standard."

There was another feature of the operation of the sterling standard which disguised from Germany the nature of the currency standard she had joined. Britain had kept the price of gold at the artificial figure of £3 17s. 10½d. per ounce for fifty-six years. It had never departed from that figure within the memory

of any living statesman or financier. It was regarded as a natural price of gold, and it never crossed the minds of the German statesmen that in going on to "the gold standard" they were equating the mark to an artificial value of gold established by Britain, and maintained at that artificial value by the incessant supervision and watchfulness of the Bank of England. The mark, with its associated coinage, was simply the British pound sterling, adjusted to German requirements. It was the sterling standard translated into German.

British control of the international currency remained completely unaffected by the German adoption of the sterling standard. A debtor country can have little or no influence on the management of an international currency. It is the creditor countries which alone can take part in its active operation. Germany was a debtor country, without a first-class Money Market, and as such was carried as a passenger on the sterling standard.

France followed Germany's example in 1890. Like Germany, France adjusted the value of her currency to the sterling value of gold. But unlike Germany, France was a creditor nation with a well-developed Money Market, and was able to challenge the supreme control of the international currency by Britain in several respects. The French conception of currency, both national and international, is very different from that of Britain. The Frenchman has a national tendency to hoard his savings rather than invest them.

France maintains much higher gold reserves than Britain. France uses foreign investment more for political purposes than Britain. The High Protection policy of France clashed with the British policy of achieving the international balance of trade with goods instead of gold. These differences manifested themselves in a tendency for France to accumulate gold at the expense of the debtor countries. But the creditor position of France and the strength of the Paris Money Market were not sufficient to cause grave inconvenience to Britain in its control of the sterling standard. The French hunger for gold was satisfied mainly by the largely increased output of gold from the Transvaal. Beyond occasional irritating reminders that Britain was no longer in sole control of the international currency, the sterling standard went on as before. Britain still remained in control, and the settlement of the International Balance of Trade by goods rather than by gold, though rendered more difficult, was still possible.

The United States adopted the sterling standard at the beginning of the century by equating the dollar to the sterling value of gold. No difference in the working of the international currency was caused thereby. The United States was a debtor country, and the American conception of currency was much closer to that of Britain than that of the French. The sterling standard continued efficient and unchallenged, under British control, until the war brought it to an end, after a successful career for ninety-eight years.

For the last seventy years of its operation the sterling standard was managed on the whole so efficiently that its working was generally regarded as being automatic. The pretence that an international currency standard can be worked automatically has now been abandoned. The Ottawa Conference declared that the aim of monetary policy should be an international standard that would ensure the smooth working of international trade and finance. This declaration was quoted with approval and endorsed in the Currency Manifesto of the British Empire Delegates issued in July 1933. The long and successful career of the sterling standard was due (to adopt the words of the 1933 Currency Manifesto) to its "deliberate management in such a manner as to ensure the smooth and efficient working of international trade and finance."

CHAPTER VII

THE DOLLAR STANDARD

New Conceptions of Currency

THE delicate organisation by which the sterling standard, originally designed as a domestic currency for Britain, was enabled to expand into a world-wide international currency, could not withstand the shock of war in 1914. Three of the four of the leading commercial countries on the sterling standard were participators in the war, and their energies were devoted to far more pressing problems than that of the Balance of Trade. After the first shock of war had passed, the British Government was able to pay some attention to the question of the stabilisation of the pound sterling. The sterling standard of currency had vanished when the price of gold departed from the standard value of £3 17s. 10½d. per ounce. As the United States was not then a participant in the war, the dollar offered the best means of giving stability to the value of the pound. This method was adopted. Messrs. J. P. Morgan & Co., the leading bankers in the United States, were appointed the agents of the British Government, with instructions to peg the pound to the dollar at the rate of 4·77 dollars to the pound.

This course entailed a complete break with the sterling standard of the past. The pound sterling,

from being the unit of value of the sterling standard, and from being the dominant influence in the international currency of the world, was now forced to take a subordinate position to the dollar. But there was a more important change than that of the loss of power and prestige. The standard itself, the unit of value on which the sterling standard had been based, had changed. The value of gold, which had remained at the sterling value of £3 17s. 10½d. per ounce, for ninety-two years, and which had come to be regarded almost as a natural value of gold, was changed. The equation of the pound with the dollar at 4·77 dollars to the pound, changed the value of gold in British currency to £3 19s. 4d. per ounce. The gold value of the pound was no longer 20s., it was only 19s. 7d.

The change was similar to that which would have taken place in the domain of linear measurement if the yard had secretly changed its length to that of the metre. Every value was changed. Every contract, every lease, every debt, everybody's income was changed by being measured by a new standard. The new standard was a gold standard, being based through the dollar on a fixed value of gold. But it was not the same gold standard which had operated before the war. It was a gold standard with a different unit of value. It was not the sterling standard, it was the dollar standard. The primary difference between the two standards was the divergence between the units of value adopted as their basis.

Britain left the dollar standard after the war, and

the pound sterling dropped to its value as a unit of an inconvertible paper currency. The departure of Britain gave the United States a free hand to develop the dollar standard according to American currency conceptions. Commencing with a difference between the units of value, differences of methods of procedure and of objectives soon transformed the dollar standard into a system of currency widely divergent in its operation from that of the sterling standard.

The divergent currency policies of Britain and the United States were due to their different outlook on the international aspects of trade. Whereas foreign trade absorbed about 20 per cent of the output of of British industry, the proportion in the United States is about 5 per cent. Consequently, whereas the management of the sterling standard had been primarily directed towards ensuring its international correctitude, that of the dollar standard was directed towards its internal efficiency. The British banking system, from its inception, had always been greatly occupied with the international, rather than the domestic aspects of trade. On the contrary, the banking system of the United States was primarily occupied with the internal development of its backward states and territories.

The divergence between the two currency policies can best be illustrated by the different meaning given to the term "currency stabilisation" in Britain and the United States. In Britain, "currency stabilisation"

means its stabilisation internationally, the stabilisation of the foreign exchanges, keeping the currencies of all nations in step with each other. In the United States, "currency stabilisation" means internal stabilisation, the stabilisation of the price level in order to prevent price fluctuations from year to year. These divergent meanings of the word "stabilisation" were subsequently destined to wreck the World Economic Conference of 1933. But long before 1933 they had been the cause of making the dollar standard of currency a standard completely divorced in its operation from the sterling standard which it had superseded.

The degree to which the administration of the sterling standard had been dominated by international considerations can best be appreciated from the following extracts from the evidence given by Mr. Montagu Norman, Governor of the Bank of England, to the Macmillan Commission:—

> The main consideration in connection with movements of the Bank Rate is the international consideration.
>
> What is called the gold standard is the cement by which it (that is, the international machinery) is bound together.
>
> We are subject to whatever conditions may dominate the international position.
>
> Over the last period of years, the international system has undoubtedly been the predominant consideration.
>
> During the last few years there has been no period when we have not had continuously to face difficulties due to the international position.
>
> Especially over the last few years so far as the international position is concerned—certainly until the last few weeks—we have been continuously under the harrow.

Such quotations might be multiplied indefinitely. In its administration of the dollar standard, the United States repudiated emphatically the international considerations described above by Mr. Montagu Norman. The United States refused to be dominated by the international position. The United States refused to allow the international system to be the predominant consideration. The United States, in short, refused to place American industry "under the harrow."

The fundamental divergence between the dollar standard and the sterling standard can best be appreciated in the following passage from the Statement of Evidence presented by the Federation of British Industries to the Macmillan Commission:—

> So far as the U.S.A. is concerned, the Federal Reserve Board, as far back as 1923, openly proclaimed its deliberate abandonment of the automatic pre-war gold standard with its regulation of the volume of credit by gold; and the substitution of a system of credit control designed primarily to promote the "national" industrial and commercial development of the United States.

The distinction between the dollar standard and the British operation of the sterling standard is herein clearly outlined. The British conception was that of an international standard dominated by international interests to such an extent that British interests were allowed to remain "under the harrow" in order to ensure the success of its operation. The dollar standard, on the contrary, was "designed primarily to promote the national industrial and commercial development of the United States."

The distinction is also emphasised in a most illuminating manner by another witness before the Macmillan Commission, Sir Robert Kindersley, in the following two passages from his evidence:—

> Although New York professed to be on the gold standard, she never really allowed the gold standard to work properly.

And:—

> America went on her bended knees, almost, to the rest of the world to adopt the gold standard—but no sooner had she got them to adopt it than she refused to allow it to work.

The confusion was due entirely to the lack of appreciation that the dollar standard was a completely different standard from the sterling standard. America was not really refusing to work the gold standard. She was working a gold standard, the dollar standard, on her own lines, which were very different from the working of the sterling standard. The difference in the actual working of the dollar and the sterling standards was most apparent in their respective treatments of the debtor nations. The sterling standard had protected the debtor nations from a drain of gold for seventy years (1844–1914). Under that protection the development of the backward countries of the world had rapidly proceeded and international commerce had expanded enormously. The dollar standard withdrew that protection. The dollar standard effected a complete reversal of the sterling policy of settling the International Balance of Trade with

goods instead of with gold. The dollar standard established and stimulated a drain of gold from the debtor countries of such a volume that the drain to Britain in the early days of the sterling standard was a mere trickle in comparison. The dollar standard was not only a different standard from the sterling standard. It was an antagonistic standard. Its operation defeated the objects which the sterling standard regarded as vital. The dollar standard was not in a state of benevolent neutrality as regards the sterling standard, it was in a state of active and aggressive hostility.

The dollar standard was not only hostile to the sterling standard in its policy of draining the gold resources of the world, to accumulate huge and unnecessary gold reserves in the United States; it was hostile in its method of dealing with its gold reserves. The sterling standard policy is described in the Macmillan Report in the following terms:—

> Countries which are losing gold must be prepared to act on a policy which will have the effect of lowering prices, and countries which are receiving gold must be prepared to act on a policy which will have the effect of raising prices.

The United States deliberately refused to adopt the price policy here enunciated, with all the force of the imperative "must." It was this refusal to which Sir Robert Kindersley referred when he stated that the United States refused to work the gold standard. The dollar standard was not operated on the principle

that its price policy should be determined by the inflow and outflow of gold. It was operated on the very divergent policy of stabilising the price level in the United States quite independently of the international movements of gold. If prices in the United States showed a tendency to fall, credit was expanded in order to raise them. If prices showed a tendency to rise, credit was contracted in order to keep them steady. The international position, and the interests of other nations were ignored in these operations.

The Report of the Macmillan Commission, although it abounds in illustrations and instances showing the essential differences between the sterling standard and the dollar standard, veils them in a cloud of diplomatic reticence. The following quotation, though of somewhat undue length, is given in order to indicate how the fundamental differences of two widely divergent currency standards were made to appear as purely chronological differences.

> The nineteenth-century philosophy of the gold standard was based on the assumptions that (*a*) the increase or decrease of gold in the vaults of the Central Banks would imply respectively a cheap or a dear money policy, and (*b*) that a cheap or a dear money policy would affect the entire price structure and the level of money incomes in the country concerned. But in the modern post-war world, neither of these assumptions is invariably valid. The growth of the practice of Central Banks, by which gold inflows or outflows are offset by the withdrawal or creation of bank credit, involves not the absence of policy, but a policy inconsistent with the rapid adjustment of relative money incomes and prices.

The half-truth contained in the above statement can be transformed into a correct description of facts, if instead of the phrase "the nineteenth century philosophy of the gold standard" the term "sterling standard" is used; and instead of the phrase "in the modern post-war world" the phrase "under the dollar standard" is substituted. The invalid assumptions and the inconsistent policies described above were not merely pre-war and post-war manifestations of "the gold standard." They were manifestations of two totally distinct standards of currency, the sterling standard and the dollar standard.

In 1923 vague rumours began to circulate that Britain was about to return to the gold standard. These caused grave apprehensions throughout the industrial and labour worlds. A period of gradual recovery from the dislocations of the war had taken place. Unemployment was rapidly decreasing. Capital and Labour had composed their post-war differences and had adjusted salaries, wages, and conditions to post-war prices. The possibility that this movement towards recovery would be jeopardised by financial manipulations caused consternation throughout the industrial community. In 1923 the apprehensions were voiced by Keynes, the eminent financier and economist, in the following trenchant warning:—

> I see grave objections to reinstating gold in the pious hope that international co-operation will keep it in order. With the existing distribution of the world's gold, the re-instatement of the gold standard means, inevitably, that we

surrender the regulation of our price level and the handling of the credit cycle to the Federal Reserve Board of the United States.

Here was an indication that the dollar standard was not only different, but more potent in its action than the sterling standard would be. Writing again on the eve of the catastrophe (February 1925) he characterised the proposal as a dangerous proceeding as follows:—

> A gold standard means, in practice, nothing but to have the same price level and the same money rates, broadly speaking, as the United States. The whole object is to link rigidly the City and Wall Street. I beg the Chancellor of the Exchequer and the Governor of the Bank of England, and the nameless others who settle our destiny in secret, to reflect that this may be a dangerous proceeding.

Equally impressive warnings of the fundamental difference between the conception of the international currency held by the United States and by Britain were given by the Federation of British Industries in its evidence to the Currency Commission in July 1924. They pointed out the series of disasters that would overtake British Industry if exposed to the "measure of drastic deflation" necessary to "the raising of the exchange value of the pound sterling to parity with the American dollar." As will be seen later, their prophecies of disaster were fulfilled in every detail.

But it was in the evidence given by the Federation to the Macmillan Commission in 1930 that the difference between the sterling standard and the dollar

standard is most insistently stressed. The centre round which the whole of its voluminous evidence, written and oral, revolved was the difference between the gold standard as operated by Britain and by the United States respectively. Although handicapped by not having distinctive terms in which to define these differences, they were stressed repeatedly One passage from the evidence given by the Federation to the effect has already been quoted. Another is as follows:—

In the period following 1920–21, the U.S. Federal Reserve Banks openly abandoned the statutory principle of "reserve proportions" (i.e. basing their credit policy on the size of their gold reserves) and substituted in its place a policy of attempting to stabilise trade and prices.

The standpoint of the Federation is most clearly expressed by Mr. Glenday, Economic Adviser and Head of the Economics Department of the Federation, in his oral evidence. Under cross-examination by Professor Gregory, another eminent economist, the following striking evidence of the divergence between the two standards emerged:—

Question.—What I want to get from you is, how you think the gold standard could be worked in the post-war period, as compared with the way it was worked in the pre-war period?

Mr. Glenday.—That is rather a difficult question to answer, because we cannot relate the gold standard of the post-war period to that of the pre-war period.

In other words, the dollar standard had no relation whatever with the sterling standard. The dollar stan-

dard, in fact, differed in every phase of its operations from the sterling standard. It was founded initially on a different unit of value. It was administered as a national standard rather than internationally. It drained gold from the debtor nations instead of permitting them to pay their liabilities in goods. It concentrated gold in a uselessly gigantic accumulation instead of distributing it throughout the world where it would serve as a widespread basis of credit and commerce. It stabilised the internal price level of the United States rather than the international wholesale price level. It ignored the duty of stabilising the foreign exchanges. It tended to pull down rather than to build up international commerce. It sacrificed the interests of the newly developing nations to the supreme interest of developing the internal prosperity of the United States.

Looking back, it seems incredible that these two diametrically opposed systems of currency were considered to be identical, and that they both passed under the same name "the gold standard." Still more difficult it is to imagine that "the Chancellor of the Exchequer, the Governor of the Bank of England, and the nameless others who settle our destiny" were deceived by the mere accident of the identity of the name into acting on the assumption that the sterling and the dollar standards were one and the same. Yet so it was. Under the delusion that "the gold standard" had an actual existence, Britain went on to the dollar standard in April 1925.

CHAPTER VIII

THE GOLD STANDARD

A Conflict of Currencies

THE international currency which brought the world to the brink of destruction in the six years 1925–31 is not really entitled to the name of "standard." It was a conflict of standards, mutually frustrating each other. There was only one common element about this conflict, and that was the current belief in the fallacy that such a thing as "the gold standard" really existed. The scientific meaning of a standard of currency, that it must be a fixed unit of value, was smothered beneath the superstition that gold itself, whatever its vagaries or the fluctuations in its value might be, was the standard of value. "The gold standard," a term embodying a fallacy, is, in default of any other possible term, the most suitable name by which to designate the conflict due to the current belief in the fallacy.

The evil consequences that would follow from Britain's alliance with the dollar standard were very clearly foretold in a remarkable document prepared by the Federation of British Industries in July 1924 (eight months before the fatal step was taken) and presented to the Currency Commission then sitting. It is one of the most astonishing examples of a prophecy of considerable length and complexity, being

fulfilled in every detail and every particular. The disasters to Britain which would follow alliance with the dollar standard, as predicted by the Federation, came true in every respect. The only point in which the prophecy failed was in its understatement. The disasters which actually occurred were more severe, more intense, and more prolonged than those portrayed in the dire forebodings of the Federation.

The evidence prepared by the Federation stated that the immediate result of the proposed return to the gold standard would imply "the raising of the pound sterling to parity with the American dollar." In the absence of any rise in the American price level, "an immediate return to parity with the dollar . . . would represent for us a measure of drastic deflation." This evidence anticipated by six years Mr. Montagu Norman's admission that the effect of the working of the gold standard had been to place Britain "under the harrow." Though lengthy, the following extract is worthy of production as a remarkable instance of prophecy fulfilled:—

> The consequences of raising the real value of our money by 10 per cent would be:—
>
> (*a*) serious temporary dislocation of trade and a probable increase in unemployment due to the effect of the certainty of a period of falling prices on producers, traders, and buyers;
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> (*b*) a severe fall in British prices involving serious loss to all holders of stocks and commodities and to all who trade on borrowed money;
>
> (*c*) a serious industrial dislocation, due to the necessity

of reducing money wages by 10 per cent, which would, in present circumstances, seriously increase the difficulty of maintaining industrial peace;

(*d*) a strong probability that a severe check would be administered to export trade since the improvement in the exchange value of sterling would be likely to precede and to move faster than the adjustment of internal prices;

(*e*) an increase in the real burden of the National Debt as a result of revenue falling with prices, while interest charges would remain unaltered.

Despite these solemn warnings from the representatives of British industry, Britain went on to the gold standard by means of what Keynes has described, in the calm serenity of a *Treatise on Money*, as "a rapid and cold-blooded income deflation."

The measure of drastic deflation commenced in advance in July 1924, the month in which the Federation of British Industries had predicted the disasters that would result from such a course. Everybody's income was reduced 10 per cent by the simple expedient of deflating until the reality of 18s. was transformed into the pretence of being 20s. This outstanding instance of "cold-blooded" currency manipulation was performed in the name of the gold standard. It succeeded in raising the pound to parity with the dollar, and Britain went on to the gold standard in April 1925.

This currency manipulation produced industrial disasters exceeding even the forebodings of the Federation of British Industries. Returning prosperity was transformed into deep industrial depression.

Diminishing unemployment was transformed into rapidly increasing unemployment. Real incomes were reduced all round by 10 per cent. Industrial peace was transformed into widespread and bitter industrial strife. Expanding exports were handicapped by an increase of 10 per cent in their export price, and forthwith began to diminish. The burden of the National Debt was increased by £700 millions.

The irony of the situation was that all these disasters were deliberately intended. They were according to plan. The Bank of England and the British Treasury knew just as well as the Federation of British Industries what would be the result of the drastic deflation introduced in 1924. It is an economic truism that deflation can only act through lowered prices, depressed trade and increased unemployment. The Macmillan Report, in a particularly gentle criticism of the action taken by the Bank of England and the Treasury in 1924, preparatory to the return to the "gold standard," states that "unfortunately, the anticipations of those who were responsible for our return to the gold standard in 1925 have to a large extent not been fulfilled." That is an extreme understatement. Their anticipations were fulfilled. They anticipated lower prices; that anticipation was fulfilled. They anticipated trade depression; that was fulfilled. They anticipated an increase in unemployment; that was fulfilled. They anticipated a general decrease in all incomes; that was fulfilled. These results were not only anticipated, they were intended.

That they were intended is clear from the following passage from the Macmillan Report:—

> Great Britain established a gold parity which meant that her existing level of sterling incomes and costs was relatively too high in terms of gold, so that, failing a downward adjustment, those of her industries which are subject to foreign competition were put at an artificial disadvantage.

The term "downward adjustment" is a euphemistic economic phrase meaning a fall in wages, a fall in profits, and a fall in incomes. Failing to achieve this "downward adjustment," British exports were put at an artificial (the term "artificial" is enlightening) disadvantage.

There was one respect in which the anticipations and the intentions of the Bank of England and the Treasury were not fulfilled. To use a phrase from the Macmillan Report, "the sacrifices which a return to gold at the old parity involved" were intended to be temporary only. They were to be rewarded by a return to the golden age, to the golden standard, which would put an end to all the preliminary tribulations endured. The permanent good time coming on the gold standard would erase all recollections of the critical ten months of preparation which had to be endured. Unfortunately, despite the sacrifices endured, the golden age did not materialise.

One phase of the preliminary preparations for the return to the gold standard has not received the attention it deserves. Unemployment is regarded in Britain with such a universal feeling of horror and dread,

that a vast and expensive system of unemployment insurance has been established to mitigate its worst manifestations. Industry and the public are heavily taxed to achieve this result. The whole wisdom and resources of the Government are supposed to be marshalled to reduce the evil of unemployment to its lowest dimensions. Yet in 1924 the Bank of England and the Treasury were permitted to embark on a course of drastic deflation which could only succeed in its object by the creation of additional unemployment. The Government was fighting against itself. One department was actively engaged in creating unemployment, while other departments were fighting unemployment by the medium of heavy taxation. Industry and the public were being bled by taxation to relieve the unemployment deliberately created by the Bank of England with the active co-operation of the Treasury.

All the sacrifices endured were in vain. The golden age never came. The Federation of British Industries was right; and the Bank of England and the Treasury were wrong. They had miscalculated in every particular. It was not that they had failed to foresee the future. They had failed to see the present and the past. They were blind to the divergent operation of the dollar standard from the sterling standard of pre-war days. They had failed to see that in adopting the gold standard they were entering into an inevitable conflict with a hostile currency system strongly entrenched in the United States.

The Macmillan Report states that the six years since the return to the gold standard "proved to be of a very abnormal character." They were abnormal because the action of the Bank of England and the Treasury made them abnormal. Never was the outlook for a return to world-wide prosperity brighter than in 1924. True, there had been unparalleled destruction during the war; there were enormous legacies of war debts and reparations to be liquidated; and the currencies of Western Europe were inflated almost to vanishing point. But on the other hand there was an unprecedented increase in the production of wealth. Mankind had achieved a dominance over nature that made the outstanding liabilities of the war trifling in comparison with the potential increase of wealth. In agriculture, in mining, in industry, in transport, greater progress was being achieved in one year than had been accomplished in a decade before the war. All that was wanted was a scientific system of currency adapted to the new conditions, just as the sterling standard had been adapted to the new conditions of a previous century. Excellent progress was being made in 1924. Sterling, even on an inconvertible paper standard, was gradually resuming the benevolent dominance it had exercised before the war. Just as the Pound Sterling, free from gold, was about to achieve a second revolution that would bring even greater benefits to mankind than it had brought in 1816, its activities were curbed by its being bound with golden chains to a hostile and alien currency.

The six years of "very abnormal character" (according to the Macmillan Report) divide themselves naturally into two periods of three years each. In the first period, 1925–28, two hostile systems of currency based on sterling and the dollar struggled for supremacy. In the second period, 1928–31, a third system of currency, based on the franc, hostile to both, engaged in the combat. The conflict was not rendered any the less strenuous by the fact that each combatant fought under the same banner, "the gold standard," and that each was imbued with the assurance that its interpretation of the golden rules was the one true faith.

No item in the list of disasters predicted by the Federation of British Industries was fulfilled so exactly as that which foretold "a serious industrial dislocation due to the necessity of reducing money wages by 10 per cent., which would in present circumstances seriously increase the difficulty of maintaining industrial peace." No sooner had Britain returned to the gold standard than export prices were raised by 10 per cent. The coal export trade was particularly affected. To counteract the handicap of a 10 per cent increase in the export price of coal, the coal-owners endeavoured to reduce the miners' wages by 10 per cent, exactly as had been predicted by the Federation of British Industries. The miners went on strike against this reduction, having an uneasy (and perfectly correct) feeling that the situation had been artificially engineered to their disadvantage. The

workers in other industries, knowing that their wages were threatened in exactly the same manner, joined in, and the Coal Strike became the General Strike.

But the Coal Strike and the General Strike were trifles in comparison with the disasters to come. The necessity for complete co-operation between nations if the gold standard is to work successfully is prescribed in the following passage from the Macmillan Report:—

> Therefore all gold standard countries, and particularly all important ones, are vitally interested in each other's stability. Particularly if any country in a dominating position pursues a course which may appear to suit its own interests, but is inconsistent with the maintenance of stability in the rest of the world, much damage is done, certainly to the latter, and probably in the end to the former also.

This passage describes faithfully and exactly the policy of the United States in administering the dollar standard. It was foreshadowed by Keynes in February 1925 in far more emphatic language as follows:—

> Those who think that a return to the gold standard means a return to these conditions (the pre-war currency conditions) are fools and blind. We are now the debtors of the United States. Their foreign investments last year were double ours, and their true net balance available for investment was probably ten times ours. They hold six times as much gold as we do. . . . A movement of gold or of short credits either way between London and New York, which is only a ripple for them, may be an Atlantic roller for us.

Exactly the same factors, refusal to co-operate on the part of the United States, and the immense power of the United States to create disequilibrium in the

rest of the world, are implied in the following passages from the Macmillan Report:—

> The immense growth of the United States has altered the scale, if not the terms of the problem of American-European economic relations.

And:—

> The working of the international gold standard requires, in the modern world, a realisation that the forces making for disequilibrium are very powerful.

Yet the Bank of England and the Treasury placed the industrial prosperity of Britain under the control of this enormously powerful financial country with an antagonistic currency system, and imposed heavy burdens of trade depression and unemployment in order to do so. The return of Britain to the gold standard in 1925 made her the financial vassal of the United States; or to use Mr. Montagu Norman's phrase, "so far as the international position is concerned, we have been continuously under the harrow."

Britain's position of vassalage is best illustrated by her forced assumption of the humiliating position of debt-collector for the United States. The High Protection policy of the United States prevented her debtors from paying their liabilities in goods. They had to be paid in gold. To obtain the gold there was only one free world market, Britain. The debtors of the United States therefore dumped their goods into Britain, knowing that, if they refrained from purchasing any goods from Britain in return, the operation

of the gold standard would force Britain to remit the value of the dumped goods in gold to the United States, and so discharge their debts.

This post-war operation of Free Trade under the gold standard must be very carefully distinguished from the pre-war operation of Free Trade under the sterling standard. Under the sterling standard Britain was protecting and obliging her own customers, and collecting her debts in the manner most convenient to them, by taking them in goods instead of in gold. But under the gold standard, Britain was obliging the United States, and the debtors of the United States, by taking goods in payment of their debts, and then remitting their value, in gold, to the United States. In order to do this she had to drain the world of gold, not for her own use, but to add to the useless hoards of the United States. Under the sterling standard, Britain was protecting the world from a drain of gold. Under the gold standard, she was placing the whole of the magnificent organisation of her international currency and of the London Money Market at the disposal of the United States, in order to collect all the available gold in the world and ship it to the United States.

Under the gold standard Britain was forced by the United States to pull down the splendid edifice of international confidence and international commerce which she had created in the nineteenth century on the basis of the sterling standard. She had no option. She was under the harrow. Having protected the

debtor nations of the world from the drain of gold for seventy years, she was now forced into being the active instrument in enforcing this fatal drain of the life-blood of international commerce.

Britain's position as debt-collector for the United States was not only degrading and humiliating; it was disastrous to her own industry. It was disastrous in four different ways:—

(1) Britain's internal industry was dislocated by the excess of dumping by the debtors of the United States. Dumping from her own customers was a factor that could be adjusted by mutual trading. Dumping from the customers of another nation could not be so adjusted, and it accordingly produced extreme disorganisation by introducing a far larger quantity of imported goods than could be absorbed.

(2) Debtor countries could only pay their debts to the United States in gold by intentionally refraining from buying British goods. However strong the desire to "buy British," this was negatived by the necessity of not dissipating the gold acquired from Britain with which to pay their debts to the United States.

(3) Britain's export trade was hampered extremely by the impoverishment of her customers, owing to the strength of the drain of gold from all countries to the United States, and still more by the exchange restrictions and other gold protection measures by which they sought to defend their dwindling stores of gold.

(4) Every section of British trade, industrial and

commercial, internal and foreign, was crippled and disorganised by the rigid and continuous deflation of currency and credit which the Bank of England imposed in order to attract from all sources the gold with which to maintain the constant transfers of gold to the United States.

The operation of the gold standard in this respect, and the utterly impossible position of Britain under this fourfold menace to her industries, is described in the following terms in the Macmillan Report:—

> It is not possible, even for a creditor country, to go far in the direction of increasing either its own buying or its own lending, unless the other creditor countries are moving more or less in step.

It is a magnificent tribute both to the magnanimity and to the financial strength of Britain that she continued the task here described as impossible for over six years, with the United States, and subsequently France, not only out of step, but actively acting adversely to Britain.

In August 1928 France reinforced the Anglo-American currency conflict, by adopting the gold standard and by contributing a currency devalued to the enormous extent of 80 per cent, and a conception of currency based on a national hoarding complex. France has always shown a preference for money over investment as a method of storing savings. She prefers short term investments to long-term investments, and prefers money (metallic money if procurable) to either. She tends to distrust cheques and

other forms of representative currency which serve to economise gold. She insists on a high backing of gold reserves for all currency operations. After describing in detail the characteristics of French monetary policy, the Macmillan Report stated:—

> The importance of these developments from the standpoint of the international gold standard was that they involved an enormous inflow of gold into France.

Thus, to the "enormous inflow" of gold into the United States was added an "enormous inflow" of gold into France. Britain now became the vassal of France in the debt-collecting line, as well as the vassal of the United States. France proved an even harder taskmaster than the United States in the policy of using the British conception and administration of the gold standard to drain the world of its gold. The four disastrous effects on British industry described above were now intensified by the enforced collection of debts for France as well as for the United States. Moreover, to the handicap of British exports, caused by the pound being valued at 10 per cent above its true value, was added the handicap of competition with a franc devalued from 10d. to 2d., 80 per cent below its true level.

Subjected now to a double drain of gold to both France and America, the debtor countries grew desperate. In the two years 1929–30, despite rigorous exchange restrictions and other measures (fatal to the maintenance of international trade) to protect their gold, they lost £150 millions. The Macmillan

Report stated despairingly: "It is unlikely therefore that the debtor countries can continue much longer to square their international position."

Meantime while the edifice of international commerce, constructed on the basis of the sterling standard, was being rapidly brought to ruin, American prosperity progressed by leaps and bounds. The nine years' accumulation of gold, drained from the debtor countries, formed a basis of credit for the most remarkable period of industrial progress ever known. Mass production, on a scale never before attempted, resulted in low costs, with enormous sales and enormous profits. It proceeded until the United States became a workshop, capable of supplying almost the total requirements of the world. And then the world refused to buy.

The world was ruined. The magnificent productive organisation of the United States found itself without a foreign market. It could not possibly assimilate its own production. The enormous output could only be absorbed by a world market. In creating its own prosperity, the United States, ably assisted by France, had ruined the world markets. The inevitable slump came in the autumn of 1929. It was useless to produce for a world that could not buy.

Britain, as usual, had to bear the brunt of the crisis. While France and the United States were administering the gold standard on policies that protected themselves, as far as possible, from the reper-

cussions of the international position, the Bank of England was administering it on a policy that made it sensitive to every external event. In February 1929, in the efficient performance of debt collection on behalf of France and the United States, the Bank Rate was at the deflative level of 5½ per cent. This was a rate which gave international finance a strangle-hold on British industry. But, as if five years' continuous deflation of credit and currency had not placed Britain "under the harrow" of the international position sufficiently, the Bank Rate was raised to 6½ per cent in September 1929. This knock-out blow was felt in every factory, and mine, and mill, and shop, and household in the country.

With characteristic self-depreciation, Britain attributed to her own deficiencies the evils and disasters inflicted upon her by adhesion to a chaotic system of currency. A rage for economy set in. Britain was living beyond her means. Britain was living upon her capital. Britain's standard of living was too high, her social services too costly, her expenditure on public works too lavish. Every reason for the disasters that were occurring was given except the true one, that Britain was starving in a world of plenty through adherence to a chaotic and unworkable system of international currency.

Relief came at last. Prominent statesmen and financiers began to assert vehemently that nothing on earth would induce them to forsake the sacred cause of the gold standard. This caused an immense

feeling of relief throughout industrial Britain. Such declarations are not undertaken until the policy, in whose behalf such heroic protests are made, is doomed. The more fulsome the tributes to the effect that the gold standard was linked with the honour of Britain, and was one of the most glorious of British traditions, the nearer was the escape from "under the harrow" at hand.

The end came dramatically. In the months of July and August 1931 the Bank of England was faced with a demand for £200 millions of gold, not in the ordinary course of business, but merely for satisfying the growing Continental craving for hoarding gold. This amount was in excess of the reserves of gold held by the Bank. It was impossible in the time available to squeeze so large a sum from the impoverished debtor nations. In defence of Britain's honour, the Government cringed to France and the United States, and borrowed two sums of £50 millions and £80 millions in order to pay the debt collections which she was ruining her industries to screw out of the debtor nations. Britain's honour had sunk to such a low ebb that it was measured by her capacity to wring distress consignments of gold from the ruined debtor nations.

These were the final experiences "under the harrow." On September 21, 1931, Britain emerged from the most disastrous currency experiment that had ever brought the world to the brink of ruin. Eminent statesmen and financiers attempted to make our flesh

creep by emphasising, in funereal broadcast orations, the critical nature of the step that had been taken, and the trials and tribulations that encompassed the nation in its future wanderings in an unexplored and uncharted financial world, surrounded by unnameable currency terrors.

But our feelings refused to be harrowed. The relief was almost too overwhelming to be endured. The unexpected freedom from a seven years' bondage was almost insupportable. Keynes expressed the real feelings of Britain at her emancipation from a slavery which had become intolerable in the words:—

> Out of the ashes, the City of London will rise with undiminished honour. For she has played the game up to the limits of quixotry, even at the risk of driving British trade to a standstill. No wonder then that we feel some exuberance at the release, that Stock Exchange prices soar, and that the dry bones of industry are stirred. In many lines of trade the British manufacturer to-day must be the cheapest producer in the world in terms of gold. We gain these advantages without a cut of wages and without industrial strife.

Britain was no longer "under the harrow."

CHAPTER IX

HOARDING

The Disappearance of Gold

THERE are three traditional functions performed by money, those of providing a medium of exchange, a standard of value, and a store of savings. The sterling standard in 1816 was based on a fixed value of gold because gold was deemed to be the most suitable metal for all three purposes. This assumption was quite correct. Gold performed all three functions better than they had been performed in any previous system of currency. But during the operation of the sterling standard for ninety-eight years, the use and the relative importance of gold in carrying out these three functions was profoundly modified.

As a standard of value, the sterling value of gold at £3 17s. 10½d. per ounce, remained fixed and unchanged throughout the whole period. But as a medium of exchange, the importance of gold gradually diminished, both internally and internationally, throughout the period of the sterling standard. The use of cheques superseded the use of gold for all internal transactions other than those of the payments of wages and small personal and shopping expenses. Externally the great development of the use of bills of exchange, and the improvement of the methods of settlement of the International Balance of Trade adopted by the money

markets of the world, made gold payments between nation and nation less and less necessary. Gold had almost ceased to be an active medium of international exchange in 1914.

It was, however, with the third function of money, that of providing a store for savings, or briefly, hoarding, that the sterling standard made the greatest revolution. Hoarding money as a method of storing savings had been the traditional and almost the only method up till the beginning of the nineteenth century. An alternative method of storing up savings by means of investment had, indeed, existed from time immemorial. But it was a risky method. Its profits did not compensate for its risks for the majority of the people. It was too speculative to appeal to any except to the wealthy and to those who made investment a profession. The sterling standard, by creating both national and international confidence in its stability, and by creating new and profitable openings for investment, made this method of storing savings much more popular. Investment with the profitable accompaniments of interest or dividends, was brought within the reach of all whose savings amounted to an appreciable sum.

The ninety-eight years of the dominance of the sterling standard were marked by a gradual movement from hoarding to investment as a means of storing savings. This movement was so comprehensive that a preference for investment was regarded as the distinguishing mark of the more progressive commercial

nations of the world. A preference for hoarding, either on the part of a nation or of a social class, was regarded as a sign of a want of enterprise and commercial backwardness.

The great secret of success of the sterling standard during the nineteenth century was the economy it effected in the use of gold. By the confidence it engendered, it facilitated the use of representative money such as cheques and bills of exchange. The utility of gold as a medium of exchange was greatly multiplied by these means. The growth of the world's wealth during the nineteenth century was, according to the best authorities, proceeding at an average rate of increase of about 3 per cent per annum. The growth of the world's stock of monetary gold during the same period averaged about 2 per cent per annum. There was therefore a deficiency of about 1 per cent per annum in the production of gold relatively to the production of wealth, a deficiency which ordinarily would have increased cumulatively from year to year. This diminished supply of gold relatively to the demand for currency would normally have forced the price of gold far above the sterling value of £3 17s. 10½d. per ounce, and so destroyed the sterling standard.

But two great economies were effected in the use of gold. As a medium of exchange it was economised by the growing use of representative money. As a store of savings it was economised by the growing practice of investment. These two economies enabled the 2 per cent per annum increase in the amount of monetary

gold to keep pace with the 3 per cent increase in the production of wealth. They equated the supply of gold to the demand for its monetary services, and so enabled the Bank of England to keep the sterling value of gold at a constant level from 1822 to 1914.

A reaction from investment to hoarding as a store for savings commenced with the war. The wild inflations of European currencies after the war, destroyed confidence in both investments and paper currencies, and greatly stimulated the hoarding of gold and silver which was a legacy from the war. But the greatest stimulus to the revival of the habit of hoarding after the war came from the most unexpected quarter. The very institutions whose primary function it was to safeguard the stability of the value of gold, reverted to the primitive practice of hoarding gold, a habit destructive of its utility as currency. The Central Banks of France and the United States, by accumulating and hoarding enormous and unnecessary stocks of gold, were curtailing the supply of currency and increasing the demand for gold to an extent that greatly affected the stability of its value. Instability of value renders any medium totally unsuitable to provide a standard for currency purposes. The hoarding of gold by the Central Banks of France and the United States has therefore had a material effect in making the continuance of the gold standard impossible by rendering its value so unstable that it is no longer an efficient measure of value.

In so far as the gold they hoarded was diverted

from the more useful purpose of providing a medium of exchange, they were reversing the process by which the sterling standard established the great volume of international commerce in the nineteenth century. The sterling standard multiplied the utility of gold as a medium of international exchange. The currency policies of France and the United States on the gold standard both curtailed the amount of gold available as a medium of international exchange, and by destroying confidence, curtailed the utility of the residue which still remained to perform active currency functions.

The currency policies of France and the United States (and of the Continental nations associated with France) greatly stimulated hoarding in another manner. They forced the debtor nations to employ exchange restrictions, gold protection tariffs and quotas, and other restrictive measures, in defence of their diminished stores of gold. By thus hampering the use of gold for the purpose of currency, investment and trade, they forced it into the alternative use of hoarding.

Up to 1930, although there was a steady increase of private hoarding, stimulated by the example of, and proceeding simultaneously with the hoarding by the Central Banks, it was not on such a scale as to impress itself noticeably on the mass movements of gold from country to country. By the end of 1929 the gold reserves in the French and the American Banks were £336 millions and £802 millions respec-

tively. In 1930 France increased these figures by £96 millions and the United States by £67 millions. In 1931 private hoarding had grown to such a scale that it was apparent in the figures giving the international movements of gold. Private hoarding in the United States in that year rose to the immense figure of £75 millions; and the three countries, France, Holland, and Belgium, besides increasing their gold reserves by £192 millions (more than twice the total production of gold for the year), added the sum of £43 millions to private hoards. In 1932 private hoarding in these three countries was increased by £79 millions, and gold reserves by £135 millions.

Thus the example of hoarding by the Central Banks was rapidly communicated to the people of these countries. The total amount of gold being hoarded (bank hoards and private hoards) was far in excess of the total annual production of gold from the gold mines of the world. It was rendered possible by insistent pressure exerted on the debtor nations to yield up their already depleted supplies of gold. The Macmillan Report mentions "distress shipments" from Spain, Argentine, Brazil, and Australia in 1930. Subsequently India came to the relief of an almost intolerable situation, and, attracted by the high price of gold obtainable, began to export her hoarded millions of gold at the rate of £50 millions per annum.

Other forms of hoarding, besides that of accumulating silver and gold, were stimulated by the general lack of confidence and the curtailment of international

investment, resulting from the currency policies of France and the United States. On the Continent, and more particularly in France, the hoarding of bank notes is now very prevalent. But a more usual form of hoarding, which has now grown to very great dimensions, is the accumulation of short loans or liquid capital beyond the amount necessary for commercial requirements. A certain quantity of such loans is required for the working of the money markets in the settlement of bills of exchange, stock market transactions, and other commercial and financial operations. They are liquid assets which can be transformed so readily into ready money, that they are now frequently referred to as being ready money. They are, in reality, ready money at one remove.

The holding of this class of liquid assets, not for the purposes of actively assisting currency and trade, but for the purpose of retaining them till a favourable moment arrives to transform them into money, is hoarding. It has exactly the same effect in curtailing investment, and in preventing gold from being available for the performance of currency functions, as the actual hoarding of gold. It has an equal effect on the instability of the value of gold. This is clearly explained in the following passage from the Macmillan Report:—

The perils of the war and the post-war period and the unfortunate currency experiences of many countries have led to a greatly increased preference for liquid assets as compared with long-term securities. Especially there has

been a tendency on the part of many countries to pile up liquid claims in the leading financial centres, instead of embarking in foreign fixed investment or funded obligations. France, the third largest creditor country in the world, appears to have employed, virtually, the whole of her international surplus during the last three or four years in the purchase of gold and short term liquid claims; whilst the attitude of the investors of the United States, which is now the second largest creditor country next after ourselves, has fluctuated violently. The effect on prices internationally of an increased preference for employing resources in the purchase of liquid claims, including gold, is the same as that of hoarding in a primitive community.

The total amount of this form of hoarding—by means of short-term liquid assets—is even greater than the amount of hoarded gold. Conservative estimates place the amount of short-term liquid securities at the figure of £2,500 millions, that is, more than the total amount of monetary gold in the world. This means that the whole of the monetary gold of the world is more than mortgaged to the holders of these securities, the date of possible foreclosure ranging from one day to three months. In so far as they are utilised for legitimate commercial and financial requirements, they cause no difficulty, the maturities being balanced by renewals and by new issues. But in so far as they are used for hoarding, and this applies to by far the greater proportion of them, their effect is, as the Macmillan Report states, "the same as that of hoarding in a primitive community."

A special article in *The Times* of October 6, 1933, indicates that this particular form of hoarding alone

(by means of short-term investment) is quite sufficient of itself to preclude the stabilisation of the exchanges by a return to the gold standard. The following brief condensation indicates the nature of the obstacle it imposes to such a return:—

> The course of foreign exchanges is now governed mainly by the movements of short-term capital, capable of being transferred at short notice from one country to another. These ready-money balances were estimated two years ago to reach the sum of about ten billion dollars. Besides the ready-money balances actually in being, there has come into existence since the war a huge additional volume of Government securities of Great Britain, France, and the United States. The total mass of capital transferable at short notice is thus raised to a figure in comparison with which the normal trade balances of the world are insignificant, and which is far in excess of the total amount of monetary gold in existence. The existence of this enormous mass of ready money—which has no fixed policy of domiciling itself permanently in any one country, but runs from one to the other as prudence or panic dictates—makes it idle to suppose that exchanges can be stabilised by a general return to the gold standard.

A third form of hoarding, that of placing savings in fixed deposit in a bank, instead of investing them as capital, is regarded by Keynes as the most typical form of hoarding money in an advanced community, as will be seen from the following passage:—

> The choice between hoarding and investing, or, alternatively the choice between "bank deposits" and "securities."

This form of hoarding is interesting as the form which appeals most to the British temperament. It

is a further remove from the crude hoarding of gold and silver than short-term securities. But the effect is the same. It limits the amount of currency and credit available for the active pursuit of trade and investment. The amount of hoarding in Britain only, effected by the method of fixed deposits can be estimated by the fact that the proportion of bankers deposits actively utilised in advances to merchants and manufacturers was 55 per cent in 1930. The proportion has now fallen to about 35 per cent. This difference of 20 per cent of the total deposits loaned out in advances to traders and manufacturers, represents the amount withdrawn from active investment and hoarded as passive bank deposits.

The nineteenth century, under the influence of the sterling standard, witnessed a gradual weaning of the world from the primitive passion for hoarding to the more highly developed method of investment, for the storage of savings. Continuing for ninety-eight years, the change effected was considerable in its cumulative total. But a reverse movement from investment back to hoarding has proceeded at a much more rapid rate for the past nineteen years, stimulated by four influences, the war, the post-war currency inflation on the Continent, the hoarding by Central Banks, and the currency conflict waged under the banner of the gold standard. The reaction to hoarding has taken three forms, the crude hoarding of currency, the respectable middle-class form of fixed deposits, and the commercial form of short-term securities.

It has reached at the time of writing (the autumn of 1933) a pitch of intensity never before experienced. The crude hoarding of gold is not only absorbing every ounce of gold being produced by the gold mines of the world—it is absorbing the gold being de-hoarded by India at the rate of £50 millions per annum. At the same time, every particle of monetary gold, whether in the vaults of the banks, or in private hoards, is mortgaged twice over to the holders of fixed deposits and short-term securities.

The counterpart of the vast volume of hoarding of money is the equally vast volume of accumulated hoards of unsaleable commodities. The amount of purchasing power set free by the productive process is exactly equal to the amount of wealth produced. That is a truism. The selling price of a commodity is exactly equal to the purchasing power distributed in the course of its production in the form of rent, interest, wages, salaries, and profits. If the purchasing power so set free is completely expended in consumption and investment a state of stable but progressive equilibrium is achieved. The stable equilibrium is achieved by the purchasing power absorbing all the wealth produced. The progress is achieved by the proportion of purchasing power which is absorbed in investment.

But hoarding upsets the stability of this ordered progress. Hoarding sterilises a certain amount of the purchasing power which would otherwise equate with production, being spent either in the form of con-

sumption or investment. The absence of purchasing power sterilised and placed into cold storage by hoarding, means that an equivalent volume of commodities produced are unsaleable. The surplus hoards of wheat, coffee, rubber, tin, copper, and many other commodities equate with and are the counterpart of the hoarded millions of gold, short-term securities, and fixed deposits. Over-production is a misnomer for the under-consumption caused by hoarding; under-consumption in its widest sense, under-consumption of the commodities produced for use, and under-consumption of the commodities which should be utilised for investment; or, more briefly, underconsumption and under-investment.

The outward and visible sign, and to some extent the measure of the volume of hoarding, is the appreciation of the value of gold. The appreciation of the value of gold in terms of commodities since Britain went on to the gold standard in 1925 has amounted to 5·4 per cent in 1926, 2·3 per cent in 1927, 4 per cent in 1928, 7·6 per cent in 1929, and 16·5 per cent in 1930. These violent fluctuations demonstrate that there was no such thing as a stable standard of currency during the nominal operation of the gold standard from 1925 to 1931. Instead of a stable unit of value as the basis of currency, there was a violently fluctuating basis which distorted rather than measured the value of commodities. This destruction of the currency standard was primarily due to the hoarding of gold by the Central Banks of the United States

and France. By hoarding gold and short-term securities they depleted international currency, and by curtailing the supply caused continuous fluctuations in its value. The fluctuations of the currency standard have been accelerated recently by the rapid spread of private hoarding.

So unreliable and impossible had gold become as a measure of value, that as soon as Britain departed from the gold standard in 1931 sterling began to displace gold as a much more reliable measure of value and a more efficient medium of exchange. Sterling became an inconvertible paper currency, traditionally regarded as the most unreliable of all currencies. But it rapidly became a much more stable measure of value than gold. This fact was carefully explained in the following terms by the Rt. Hon. R. McKenna, Chairman of the Midland Bank, at the Ordinary Meeting of Shareholders in January 1933:—

> If we give any true meaning to currency stability, we shall find that sterling, which is by far the most important of the currencies detached from gold, has shown, since it acquired independence, much greater stability than the dollar. (N.B. the dollar was then on the gold standard.) On balance the pound, measured by its purchasing power over commodities other than gold, has remained fairly constant. Gold, on the other hand, has almost continuously increased its purchasing power, and buys roughly 15 per cent more goods and services now than in September 1931.

Since Mr. McKenna made this speech gold has become even more unstable. The 15 per cent increase in the value of gold, mentioned by Mr. McKenna,

was due entirely to hoarding and not to any demand for currency. Gold had practically ceased to perform currency functions. It was demanded solely for hoarding, and the demand for this purpose was so intense that its value was forced up by 15 per cent in sixteen months. Gold has still further appreciated by 8 per cent (from £6 3s. 8d. to £6 13s. 5d. per ounce) at the time of writing (October 1933). But so intense is the demand for hoarding, that even at this inflated value, a premium ranging from 1d. to 9d. per ounce above the parity value of gold is usually quoted.

During the past three years the range of the fluctuations of the value of gold has been equal to 60 per cent of its value. Fluctuations of this rapidity, or of this degree, were previously unknown, even in the days of the unscientific silver standard. The remarkable achievement of the sterling standard in the nineteenth century, the provision of a stable currency, has been lost under the gold standard since 1925. The immense financial and commercial problems of the twentieth century are being hampered in their solution by an international currency less stable and less efficient than the silver currency of the eighteenth century. It is neither sufficiently adequate in quantity, nor sufficiently stable in value, to perform two of the three functions which money is intended to fulfil, those of providing a standard of value and a medium of exchange. The all-round utility of money has been sacrificed to one only, and that the least valuable of its three functions, that of hoarding.

During the past nineteen years, therefore, one of the three functions of money, that of providing a store for savings, has operated in a manner antagonistic to the due performance of the two remaining functions, those of providing a standard of value and a medium of exchange. During the nineteenth century, the passive function of money, that of hoarding, or providing a store of savings, gradually declined, and enabled the active function, that of providing a medium of exchange, to operate much more freely and effectively. The growing use of the term "currency," meaning money in its active or circulating capacity, indicated that money was being considered primarily from the point of view of its efficiency as a circulating medium, and that its static function of providing a store of savings was being relegated into the background, and was being superseded owing to the growth of banking and investment.

But it is now no longer correct to regard money primarily as being concerned with the provision of currency. The demand for money, not for the purpose of industry or commerce, but for the passive function of hoarding, has tended to overshadow its active function, that of providing a medium of exchange. The recent growth of the use of money for hoarding has caused a severe deflation of the amount of money available for currency, using the term "currency" to denote the portion of the available supply of money devoted to the active functions of exchange and investment. This deflation is not confined merely

to the hoarding of gold. It has expanded till it includes such forms of accumulation as short-term investments and bankers' deposits. The use of a vast and a growing proportion of the available money of the world for the purpose of hoarding, and the short-term mortgages held over the whole of the world's monetary gold, have caused a serious depletion of the amount of currency available to finance the distribution of the wealth created by industry. With an extremely rapid increase in the amount of wealth to be distributed, requiring a proportionate increase in the amount and efficiency of currency, hoarding has caused a severe curtailment of the amount of currency available to effect its distribution with efficiency.

Hoarding has not only reduced the amount of currency available as a medium of exchange; it has also prevented money from performing its remaining function, that of providing a stable standard of value. The experience of the Bank of England, from 1822 to 1914, demonstrated that it is possible to maintain a stable value of money through a prolonged period of change and progress, provided that the function of hoarding is not permitted to assume a dominating position in the usage of money. So long as money was primarily devoted to the purposes of exchange and investment, the amount required was capable of being estimated and its value controlled. But now that money is being devoted in incalculable quantities to hoarding, the amount required can neither be foreseen nor controlled. The experience of the world

since 1914 has demonstrated that it is quite impossible to preserve a stable value of money while it is being utilised in quite unforeseeable quantities for the purposes of hoarding.

In order to supply the modern world with the amount of currency necessary for the vast volume of transactions, national and international, which it is required to perform, it is necessary completely to dissociate it from the function of hoarding. The duties which a modern currency is called upon to perform are too comprehensive and too vital to the prosperity of the world for them to be jeopardised by the sterilisation of a large proportion of its volume for irrelevant purposes. The storing of savings and the transactions of exchange are functions that have now grown too antagonistic to each other to be satisfactorily performed by one medium. There must be a specialisation of equipment to perform these two widely diverse functions. In so far as the precious metals are required for hoarding purposes, they are unsuitable for currency purposes. The intrinsic value of gold, which makes it so valuable for hoarding, is a positive handicap for its use as currency.

This seeming paradox, that the intrinsic value of gold makes it unsuitable for use as currency, is demonstrated by the action of all nations of the world in withdrawing it from currency. Gold has ceased to be used as an internal currency throughout the world. The Bank of England nearly brought the commerce and industry of Britain to a standstill by continuing

to use gold as a medium of international currency, when every other Central Bank in the world was using it as a medium for hoarding. The experience of the gold standard from 1925 to 1931, and this has been confirmed by experience since 1931, demonstrated that "hoarding" and "currency" are two functions that can no longer be performed effectively by the same medium. The standard of value of the currency must be fixed in some medium that cannot be sterilised, or cornered, or hoarded.

Hitherto, apart from providing a standard of value, money has been called upon to provide two totally distinct and antagonistic services; one static and passive—the storage of savings, and one active and circulating—the financing of sales and purchases. There has always been a conflict in the performance of these mutually antagonistic services, but it is only within recent years that the conflict has produced a completely intolerable situation. The growing use of the term "currency" indicates that the active function of money is of so special a nature, and so distinct from the merely passive function of money, that the two should no longer be permitted to have injurious reactions on each other. The amount of active currency needed to finance the wealth production of the world, should not be governed, as it now is, by the degree of panic which prevails among the relatively backward nations. It should be regulated by one sole positive criterion. It should be the amount required to equate the demand of the world for commodities

required for immediate consumption and for capital provision for the future, with the supply of wealth actually being produced. That amount can only be supplied by making its determination and provision the supreme aim of every currency authority in the world, completely free from the distinct and irrelevant objective of providing a medium for the storage of savings.

The Macmillan Report set the fashion of paying a tribute of superstitious reverence to the gold standard, while making practical proposals for its supersession. This practice has now become popular. Declarations, manifestos, and resolutions expressing unbounded confidence in the gold standard, provided certain conditions are satisfied, have been frequent. If the conditions are examined, they are found to be quite impossible of fulfilment, rendering the expressions of loyalty to the gold standard unmeaning. The conditions, if specified, imply such impossible contingencies as the abandonment of protection by France and the United States, the distribution of the gold hoards of the American and the Continental Central Banks, or an agreement between the currency and commercial mentalities of Britain, France, and the United States.

But, though these are impossible contingencies, and the gold standard may be regarded as dead and gone, if its restoration depends on their realisation, there are infinitely more insuperable obstacles than these to a restoration of the gold standard. Among these

obstacles may be mentioned the bitter memories of the leaders of industry and of labour of the seven years "under the harrow," which they endured as a sacrifice to the gold standard. The contemptuous references to the incompetence of the British manufacturer and to the laziness and greed of the British workman, as being responsible for disasters now known to have been due to the gold standard, have not been forgotten. There is an unshakable conviction in the minds of the leaders of industry and of the workers alike that the seven years of depression and humiliation from 1924 to 1931 were artificially induced, and artificially prolonged, by the Bank of England and the Treasury in order to restore and maintain the gold standard. This conviction has been strengthened and confirmed by the revival of British industry since Britain left the gold standard, while the United States, through remaining on the gold standard, collapsed ignominiously.

Any statesman, whether Conservative, Labour, or Liberal, who attempted to translate his lip-service to the gold standard into positive action, would find that he had selected the one issue in politics which would unite the employers of labour and the trade unions in a fierce and determined agitation to defeat his object. Politically, the restoration of the gold standard is about as feasible as the restoration of Queen Anne.

But far more impossible than any of the obstacles yet enumerated is the revival of the passion for hoarding. Hoarding has been stimulated and fostered

for nineteen years, till now it has reached a pitch of intensity that cannot be controlled. It will take many years of slow growth of confidence to transform the now strongly established practice of hoarding back into the habit of investing. The work of stimulating the growth of investment performed by the sterling standard in the nineteenth century must be re-done. During this slow period of recovery, the value of gold will be uncontrollable, owing to the volume of hoarding. It is quite possible for the Central Banks to control the value of currency. But for them to attempt to control the value of the immense hoards which have been accumulated, or the demand for increased hoarding, would involve such a destruction of confidence that it need not be contemplated. For the present, and for as long a time as can be foreseen, hoarding, and not the Central Banks, will govern the value of gold, and render a fixed value, such as was adopted as the basis of the sterling standard, quite impossible.

Those who wish to restore the gold standard will be faced with an extremely difficult problem created by hoarding. Where is the gold necessary to form the basis of the gold standard to be obtained? None is available. It is all either hoarded or mortgaged. There is no free gold. Every ounce of gold in the banks is mortgaged two or three times over to hoarders in one form or other. Every ounce of gold now being produced is being hoarded as fast as it reaches the market. Though the gold reserves of the United States are four times as great as are necessary for currency

purposes, they cannot be released as they are all mortgaged. So is the gold in the Central Banks of Paris, Brussels, and Amsterdam. A gold standard, founded on gold mortgaged up to the hilt, at a gold value dictated by hoarding rather than by the demand for currency, would neither conform to tradition nor obtain the confidence adequate to make it a secure basis for an international currency. In short, all practical proposals for the restoration of the gold standard will have to await such a transformation of the established practice of hoarding, as cannot at present be either predicted or anticipated.

Since the above chapter was written, the issue of the French Government loan of ten billion francs on January 5, 1934, has afforded an opportunity to estimate the intensity of hoarding now prevalent in France. M. Georges Bonnet, the French Minister of Finance, in his preliminary statement introducing the loan, mentioned that 30,000,000,000 francs are now hoarded in France in the various forms of gold, bank notes, and swollen bank deposits. Enormous as this figure is, it must be supplemented by the amounts of two additional forms of hoarding, both particularly popular in France—short-term loans and gold held in England on French account. If the figures for these two forms of hoarding could be added, the large figure given above as an estimate of private hoarding in France would be greatly increased.

CHAPTER X

STABILISATION

The Word that Wrecked the Conference

THE Christian world, at a very early stage in its career, was split in two by a dispute over the meaning of one word. The World Economic Conference of 1933 was brought to naught by a dispute over the meaning of one word—Stabilisation. To the European mind currency stabilisation meant the stabilisation of the foreign exchanges. To the American mind, familiar with the working of the dollar standard, stabilisation meant something quite different, namely stabilisation of prices. It is significant of the paralysis which the term gold standard produced in the minds of all who acknowledged its sway, that, even in 1933, this fundamental difference between the working of the sterling and the dollar standards was not understood or appreciated.

The double meaning of the word "stabilisation" as well as the prevailing ignorance that it had a double meaning, is best illustrated by two passages from Mr. Chamberlain's speech on July 10, 1933. He was explaining to Parliament (without understanding it in the least) the cause of the breakdown of the Conference. The two passages are:—

In his message to the Sovereigns and Presidents of fifty-four nations participating in the World Monetary and

Economic Conference in London, President Roosevelt said that the Conference must establish order in the place of the present chaos by the stabilisation of currency.

And:—

As to the desirability of some permanent stabilisation and ultimate stabilisation, he did not think that there could have been any difference among the delegates. The quotation he had already read showed what an important place it took in the mind of Mr. Roosevelt only a short time ago.

Mr. Chamberlain is here suggesting that the breakdown of the Conference was due to President Roosevelt's inconsistency in first advocating stabilisation, and then refusing to agree to it, when put forward as a definite proposal. But there was no inconsistency. The stabilisation which President Roosevelt advocated was the stabilisation of prices. The stabilisation which he rejected was stabilisation of the foreign exchanges. Mr. Chamberlain's inability to see the difference in the two meanings, even after it had caused the breakdown of the Conference, is typical of the inability of British statesmen to appreciate the different principles on which the sterling standard and the dollar standard had been worked.

It was not President Roosevelt's inconsistency which wrecked the Conference. The Conference was wrecked long before it ever met by the preponderance of French influence in the preparation of the Agenda. France was determined to make the Conference an instrument for the restoration of the gold standard, and to wreck the Conference if she failed in securing

this object. Despite the departure of the United States from the gold standard, President Roosevelt's message to the fifty-four nations concerning the stabilisation of currency was misunderstood, either wilfully or through ignorance, and interpreted as meaning that the United States would be willing to agree to a temporary stabilisation of the dollar with sterling and with the franc.

The Macmillan Commission must be held responsible for the prevailing ignorance of the double meaning of the word stabilisation. The Macmillan Report had recommended a complete revolution in the British currency system, involving a departure from the traditional gold standard. Among other things it recommended a departure from the traditional European meaning of the word stabilisation, and the adoption of the American meaning. It defined the traditional European meaning as follows:—

> The primary object of the gold standard is to maintain a parity of the foreign exchanges within narrow limits.

But its recommendation for the future currency system is proclaimed in the following revolutionary terms:—

> The main objective of Central Banks, acting in co-operation in the management of the international gold standard, should be to maintain the stability of international prices both over long periods and over short periods.

Both systems were to be called the gold standard, but the "primary object" of the past system was "the

parity of the foreign exchanges" while the "main objective" of the future system was to be "to maintain the stability of international prices." The issue which broke up the World Economic Conference in 1933 had thus been definitely settled two years previously; and, what is more, definitely settled in President Roosevelt's favour, by the Macmillan Report.

Instead of boldly proclaiming the revolutionary nature of its proposals, the Macmillan Report camouflaged them by placing in the forefront of its chapter containing "Proposals Relating to International Monetary Policy," as its first objective, the recommendation "that the country should continue to adhere to the international gold standard at the existing parity." The chapter then proceeded to outline, at great length and in great detail, a policy completely inconsistent with adherence "to the international gold standard at the existing parity." The words "stability" and "instability" occur with great frequency throughout the chapter, and they are used with the meaning of the term as used by President Roosevelt (stability of prices) and never once in Mr. Montagu Norman's meaning of the stability of exchanges. The conclusions of the Macmillan Commission at the end of the chapter of its Report entitled "Proposals Relating to International Policy" are embodied in a very lengthy paragraph commencing: "We now venture to state our conclusions in summary form as follows." These conclusions, occupying a page and a half of closely printed matter, make not the slightest reference to

the stability of the foreign exchanges. They are concerned with the following objectives:—

1. Stability of international prices.
2. Stability of investment and of new enterprise.
3. Co-operation of Central Banks.
4. Autonomy of Central Banks.
5. Avoidance of large gold accumulations.
6. Control of long- and short-term investments.

The story of this attempt to camouflage a series of revolutionary proposals under the pretence of adherence to the gold standard is partly revealed in the Report. It is admitted that some of the members of the Commission thought that the return to the gold standard in 1925 had been a mistake, and that a complete break with the gold standard should be recommended. These members, though unable to carry the Commission with them, succeeded to this extent, that revolutionary proposals should be made which involved the complete abandonment of the gold standard, but that they should be put forward in such a manner that they would appear to be merely modifications of the gold standard.

This course was adopted. The mood in which Part II of the Macmillan Report (the part containing its constructive proposals) was written, is exposed with savage irony by one of the Members of the Commission, in the following passage from Keynes's *Treatise on Money*:—

To-day the reasons seem stronger—in spite of the disastrous inefficiency which the international gold standard has worked since its restoration five years ago (fulfilling the worst fears and gloomiest prognostications of its opponents) and the economic losses, second only in amount to those of a great war, which it has brought upon the world—to reverse the order of procedure; to accept, substantially, the *fait accompli* of an international standard; and to hope for progress from that starting point.

In other words, the gold standard has worked with disastrous inefficiency for five years, it has fulfilled the worst fears of its opponents, it has inflicted economic losses comparable with those of a war. But it exists. It exudes the odour of sanctity. Let it be accorded the due meed of reverence demanded by its devotees. Let us pretend to accept it, make the best of an extremely bad job, and patch it up into some sort of a workmanlike system.

This is the spirit in which the Second Part of the Macmillan Report was written, a spirit of "Let's pretend." The following is perhaps the best example of the spirit of "Let's pretend" contained in the Report:—

But there can be little or no hope of progress at any early date for the monetary system of the world as a whole, except as a result of a process of evolution, starting from the historic gold standard. If, therefore, this country were to cut adrift from the international system, with the object of setting up a local standard with a sole regard to our domestic situation, we should be abandoning the larger problem.

In this passage are three examples of sheer pretentious fustian. The First Part of the Report had

demonstrated that the historic gold standard had been completely destroyed by French and American practices, and that it could not possibly provide a starting point for a new system of international currency. Secondly, the gold standard itself had not been established in 1816 "as the result of a process of evolution" from the previously dangerous inefficient silver standard. It had been established, in the form of the sterling standard, by a revolutionary "cut-adrift" from the existing inefficient currency. So in 1931 "the only hope of progress" was a revolutionary "cut-adrift" from the even more disastrous inefficiency of the gold standard which the Macmillan Report had demonstrated.

But it is in its suggestion of the results of Britain cutting adrift from the international system that the ineptitude of the above passage is most apparent. The suggestion that if Britain abandoned the gold standard the pound sterling would degenerate into a "local standard with a sole regard to our domestic situation" was made in defiance of the teaching of history and of all canons of probability. It was falsified within three months of its publication. It was camouflage of the flimsiest nature.

A pretence, so flagrantly obvious, was certain to fail. Lord Bradbury, the die-hard gold standard enthusiast on the Commission, tore away the flimsy veil of camouflage and exposed the true inwardness of the revolutionary nature of the proposals contained in the Macmillan Report. He refused to commit him-

self to what he knew would mean the supersession of the gold standard, and in a Memorandum of Dissent, expressed his opinion forcibly as follows:—

> Such a proposal really means the substitution of an index figure for gold as the standard of value, and the new unit of value would, if the proposal were adopted, be better represented by a counter to be issued by a trustworthy international authority. The world would then be saved the labour and expense of gold mining and the Central Banks the worry of having perpetually to devise expedients to adjust the value of that no longer necessary commodity to the value of that new unit.

These are the proposals of the Macmillan Commission reduced to their baldest terms. "The substitution of an index figure for gold, as the standard of value." "The new unit of value . . . better represented by a counter to be issued by a trustworthy international authority." Gold "a no longer necessary commodity." These form the actual substance of the Macmillan Report beneath the camouflage of pretence under which they were veiled.

The Macmillan Report fell flat. The British public is not accustomed to go to a Memorandum of Dissent, relegated to page 263 of a voluminous report, to ascertain what a report really means. Having skipped the historical and analytical portions of the Report, it lighted on objective (1) of the Commission's proposals which read:—

> That this country should continue to adhere to the international gold standard at the existing parity.

That was enough. It read no more. Nothing doing.

The mountain had been in labour and had not even produced a mouse. So far as the Macmillan Report was concerned, it appeared that the six disastrous years of gloom and depression "under the harrow" were to continue indefinitely. The tragedy of the Macmillan Report was that the superficial pretence it adopted to lull the orthodox to sleep, was accepted by the public as a reality; the valuable proposals for a policy as revolutionary and effective as the currency policy of 1816, were shrouded too closely beneath a heavy pall of superstitious orthodoxy to emerge from their obscurity.

The prophetic powers of Lord Bradbury did not prove equal to his analytical ability. In the next paragraph to that in which he gave his valuable analysis of the Macmillan proposals, he stated: "I doubt whether the proposal will come within the range of practical international politics during the lifetime of the youngest of us."

This prophecy proved to be absurdly wrong. The proposal which he relegated to a far-distant future beyond the "lifetime of the youngest of us" was the predominant issue of international politics within three months from the date on which it was written. Within one year it was accepted as the policy of the British Empire at the Ottawa Conference. Within two years it wrecked the most powerful and the most representative World Conference ever assembled.

The failure of the Macmillan Commission to influence public opinion is of importance because

it led inevitably to the failure of the World Economic Conference. Had the Macmillan Report placed its main objective "to maintain the stability of international prices" in the right perspective, then the confusion of the meaning of the word "stabilisation," which wrecked the World Economic Conference, would never have occurred. But the fact that the Macmillan Report had recommended that the stabilisation of international prices should be the main objective of the future currency system, never influenced public opinion, never even entered the public consciousness. Even after the World Economic Conference had been wrecked by the attempt to impose upon President Roosevelt a meaning of stabilisation alien to that to which he had been accustomed, it never even entered Mr. Chamberlain's mind that President Roosevelt's meaning of the word in the sense of stabilisation of prices had been recommended by the Macmillan Report two years previously as the main objective of currency policy, and that he himself had accepted it as the working policy of the British Empire at Ottawa.

This feature of the Macmillan Report naturally attracted much attention in the United States. The Report had not spared the United States in apportioning the responsibility for the failure of the working of the gold standard from 1925 onwards. But on the issue of stabilisation, the United States had been much nearer the truth than Britain. While the Bank of England had placed Britain "under the harrow"

for seven years in a hopeless attempt to secure the stabilisation of the foreign exchanges by means of an incurably unstable currency, the Federal Reserve Board of the United States had been moving in the right direction in an endeavour to stabilise prices. The United States failed because of its limited, narrow, national outlook. It confined its efforts to the stabilisation of internal prices only, and made no efforts to stabilise international prices. Still, although there was this difference between the scope and range of its meaning of stabilisation, on the fundamental issue, whether the main objective of currency policy should be the stabilisation of prices or the stabilisation of foreign exchanges, the Macmillan Report had supported American interpretation and practice rather than the British.

There was another aspect of stabilisation considered by the Macmillan Report, destined to be a critical issue at the World Economic Conference. Should stabilisation be immediately effected or should it be postponed until conditions should be improved and currency stabilised at the improved level? On this issue the Macmillan Report is emphatic. In the following passage immediate stabilisation is characterised as being a serious disaster to be avoided:—

We are emphatically of the opinion that, even if a further fall of wholesale prices be avoided, then stabilisation at approximately the present level would be a serious disaster for all countries of the world alike; and that the avoidance of such an event should be a prime object of international statesmanship.

Thus the Macmillan Report not only revolutionised the meaning of the term "currency stabilisation," it put forward the revolutionary idea that there were other currency reforms much more urgent than stabilisation. Stabilisation of prices might be the "main objective," but it was not the most urgent objective. Remunerative prices were a much more insistent objective than stabilised prices. The manner in which stabilisation should be postponed until prices should attain a remunerative level is explained as follows:—

> A point will eventually come when, taking the world as a whole, international prices will have reached to a level which is then appropriate to the then existing levels of salaries and wages and to the burden of monetary indebtedness. When this point has been reached, monetary policy directed towards raising the price level further must, of course, cease, and there must be substituted for it a policy which has as its objective the stability of the international price level.

This passage provides a fairly clear summary of the general trend of the proposals of the Macmillan Report. Largely under pressure from the Dominion Representatives, the Macmillan proposals were made the basis of the currency policy of the Ottawa Conference of 1932. The postponement of stabilisation until a satisfactory level of international wholesale prices had been achieved, to be followed by stabilisation on a price basis rather than on an exchange basis, was the policy adopted by the British Empire at Ottawa. The failure of the World Economic Conference in 1933 provided the opportunity for the formulation of proposals that will eventually provide

as stable and efficient a currency system for the twentieth century as the sterling standard provided for the nineteenth century. A conference of delegates from fifty-four nations, most of them ignorant of the principles of international currency and finance, all of them in a state of reversion towards the barbarous practice of hoarding, was not exactly the medium to evolve an efficient international currency policy out of chaos. The confidence that creates an international currency is a very different quality from that expressed in "votes of confidence" at an international gathering. An international currency could only be created, as in 1816, by some one nation, in advance of all the others, creating a currency so stable and so efficient that it would inspire confidence. There would have been little hope of unanimity at a World Economic Conference in 1816 (if such an expedient had been contemplated), seeing that Britain had to wait seventy-four years before France, and eighty-four years before the United States followed her example.

The supreme courage shown by Britain in departing from the gold standard in 1931, and the intellectual ability (not the courage) of the Macmillan proposals, marked out Britain as pre-eminently the country to take the initiative in creating a new international currency standard. Moreover Britain was infinitely stronger in 1933 than she had been in 1816, by reason of the fact that she was an Empire comprising a Union of Commonwealths prepared to co-operate in the task

of creating a new system of international currency. When the collapse of the World Economic Conference was certain, the British Empire delegates met and issued a Currency Manifesto which confirmed the action of the Ottawa Conference, in the creation of an efficient and actually working system of international currency suited to the economical conditions of the twentieth century.

Appreciating that the World Economic Conference had been wrecked over the interpretation of the word stabilisation, the Currency Manifesto of the British Empire Delegates concentrated on defining what that term actually had meant for the British Empire for the past twelve months. It might almost be called a Manifesto on Currency Stabilisation. The following is a summary of its interpretation of the scope and meaning of the term stabilisation:—

i. A rise in price levels, not stabilisation, is the most urgent need of the world.
ii. Stabilisation must be deferred until a satisfactory equilibrium price level is attained.
iii. The equilibrium price level at which stabilisation should be effected is defined.
iv. The movement of price levels towards the stabilisation point must be measured by a Price Index, not by gold.
v. The stabilisation of the exchanges depends on stabilisation of prices.
vi. Stabilisation of the exchanges is only possible with those countries adopting a common policy in regard to stabilisation of prices.
vii. Stabilisation of the exchanges within the Empire is possible, because of the uniform price policy.

viii. Stabilisation of prices and exchanges within the Empire must not be jeopardised by exchange commitments with any countries not pursuing the same price policy.

ix. Other countries, providing they pursue the same price policies, may stabilise their exchanges with the sterling currency of the Empire.

Here is a compendium on stabilisation. But it is more than a compendium. It is both a manifesto and an invitation. It is a manifesto to the world that the sterling standard has been revived on the basis of the ultimate stabilisation of the price level. Not the sterling standard of the nineteenth century, glorious as were its achievements; but a sterling standard designed to cope with the immeasurably greater wealth and the immeasurably greater problems of the twentieth century. It is also an invitation to all nations to join the newly established currency standard in a co-operative effort to stabilise their exchanges at a price level which, in the words of the manifesto, "restores the normal activity of industry and employment, ensures an economic return to the producer of primary commodities, and harmonises the burden of debts and fixed charges with economic capacity."

CHAPTER XI

THE FALL OF THE GOLD STANDARD

The End of the Conflict

INTELLECTUALLY and theoretically the gold standard was dead on the publication of the Macmillan Report. Its demonstration of the chaotic conflict of rival currency systems, which had contended for supremacy under the gold standard, and its recommendation of a currency system based on price stabilisation, which could not possibly work on a gold standard and could only work on a Price Index Standard, had only to percolate through to public consciousness and the gold standard would be no more.

But the withdrawal of Britain from the gold standard three months later, in September 1931, may more suitably be taken as the date of its collapse. It had never had a real existence. The struggle between incompatible conceptions of currency which raged from 1925 to 1931 was only entitled by courtesy to the name of standard. The defection of Britain, the only country which had attempted to work it internationally, removed all pretence that it was any longer an international standard of currency. As Sir Henry Strakosch explained to the Finance and Currency Group of the House of Commons—"the future level of gold prices is now at the mercy of the conflicting policies of the United States and France."

Neither France nor the United States had made the slightest pretence that their operation of the gold standard was actuated by international interests. The gold standard was regarded by them as a national asset, all the more valuable because British traditions and British policy were devoted to keeping the international system together, and thereby enabling them to pursue their national interests all the more effectively. Britain was working the gold standard internationally because that method suited British interests; why should not France and the United States in a similar manner adopt the method which suited their interests? This was the attitude adopted when they were reproached with not following the rules of the game. Britain's withdrawal left the gold standard as a clear stand-up fight between France and the United States for the acquisition of gold.

The end of the gold standard is implied in the following extract from the Macmillan Report:—

> It is not possible even for a creditor country to go far in the direction of increasing either its own buying or its own lending unless the other creditor countries are moving more or less in step.

The use of the phrase "not possible" indicates that the situation had become impossible. It was not possible for Britain to continue its international administration of the gold standard unless France and the United States kept in step. That is the real meaning of the above passage. France and the United States refused to keep in step. The impossible situation

became intolerable. Britain withdrew, and the gold standard died.

The end of the gold standard is even more clearly envisaged in the following passage from the Macmillan Report:—

> The difficulties have arisen through the partial failure of the two recipients (i.e. France and the United States) during the last two or three years, to employ the receipts in the way in which Great Britain had always employed hers, namely, either in the purchase of additional imports or in making additional foreign loans on long terms. On the contrary, they have required payment of a large part of their annual surplus either in actual gold or on short-term liquid claims. This is a contingency which the normal working of the international gold standard does not contemplate and for which it does not provide.

This contingency, unanticipated and unprovided for, proved fatal. It was this contingency which drained the world of its gold, which revived the practice of hoarding, which brought the world to ruin, and which caused Britain to leave the gold standard. It was this contingency to which Sir Robert Kindersley caustically referred when he stated that "America went on her bended knees, almost, to the rest of the world to adopt the gold standard, but no sooner had she got them to adopt it than she refused to allow it to work." The gold standard died because the United States, and subsequently France, refused to allow it to work.

The best illustration of Sir Robert Kindersley's statement that the United States refused to allow the gold standard to work, is provided by the joint evidence

to the Macmillan Commission of Mr. Montagu Norman, Governor of the Bank of England, and Dr. Sprague, the American Banker and Financier, who at the time was officially the Financial Adviser to the Bank of England. The evidence is recorded in the Minutes as the joint evidence of Mr. Norman and Dr. Sprague, though the evidence quoted below was actually given by Dr. Sprague in Mr. Norman's presence. The following is the passage from the evidence:—

Dr. Sprague: . . . You could not force the expansion of credit by any conceivable amount of importation of gold into the United States. It is perfectly feasible to sterilise £200,000,000 or £300,000,000 in gold.

Mr. Bevin: Then the function that the gold standard was intended to perform in the nineteenth century is now played out?

Dr. Sprague: It is played out in a sense until the world gets back to equilibrium.

Mr. Bevin: What guarantee is there that it will ever play its part then?

Dr. Sprague: That is, again, a point I hope to deal with.

Mr. Bevin: It is a rather useless instrument now for the purpose of regulating or forcing an equilibrium.

Dr. Sprague: I think it is.

Mr. Montagu Norman sat by while his colleague, Dr. Sprague, explained that the United States was prepared to sterilise £300,000,000 of gold rather than allow the gold standard to work, and gave his opinion that the gold standard was played out in a sense, and that it was a rather useless instrument for the purpose of regulating or forcing an equilibrium. This evidence

was given officially on behalf of the Bank of England on February 18, 1931. "In a sense" that date may be regarded as the date of the end of the gold standard.

The members of the Macmillan Commission were in no doubt as to the grave and critical position of the gold standard. After pursuing somewhat further the investigations into the refusal of the United States and France to allow the gold standard to work, the Report makes a prophetic comment that "it may be that the whole machine will crack before the reaction back to equilibrium has been brought about."

That is exactly what did happen. The machine did crack within three months from the date of the prophecy. Britain saw the futility of still further ruining her commerce and her industries in the service of a machine which France and the United States refused to allow to work, and withdrew. After Britain's withdrawal, France managed to transform the cracked machine into a fairly efficient suction pump, and used it effectually to drain every ounce of gold that was not securely protected against her acquisitiveness. But low as the reputation of the gold standard had sunk, even its most bitter critics hesitated to apply the term "the gold standard" to the hoarding machine in operation after Britain's withdrawal.

Britain's withdrawal from the gold standard was regarded by the orthodox as an act of financial blasphemy. The golden fetish had been flouted. The world at large was filled with apprehension of the

fate that would overtake Britain now that she had defied the golden superstition. But Britain was undismayed. Her exuberant expression of relief and delight at being rescued from her degrading position "under the harrow" was regarded by her believers as verging on the indecent.

There was no speedy recovery. The past seventeen years had effected a transformation from a commercial world and an investing world, into a hoarding world. The system of international confidence and commerce created by the sterling standard had vanished. On the one hand were frozen credits, frozen accumulations of gold, a frantic greed for gold, not for the purposes of currency and trade, but for hoarding, for sterilising, for storage where it could be effectually prevented from performing any actively useful purpose. On the other hand were frozen hoards of commodities, unsaleable at anything like their cost of production. Gold had practically ceased to function as a currency over the greater part of the world. The gold standard might be dead, but it had left behind a legacy of ruin, depression, and stagnation. A desperate and prolonged struggle to recover lost ground, rather than a speedy recovery, was to be anticipated.

But Britain was free; free from the intolerable oppression of a currency conflict which had sapped her industrial vitality for the past seven years; free to work out her own destiny; free to repeat the great blessing she had conferred on the world a century before, in the establishment of a stable and reliable

system of international currency. There might be ruin and stagnation all round, but Britain was no longer hampered by a captive currency in her efforts to restore prosperity.

The pound sterling revelled in its unexpected freedom. It soon found its own level as the value of an inconvertible paper currency, and promptly proceeded to assert its authority throughout the world. It repudiated at once the unworthy suggestion of the Macmillan Commission that if "cut adrift" from the gold standard it would degenerate into a local standard with sole regard to the domestic situation. The Sterling Bill of Exchange, though based on an inconvertible paper currency, proved that it could more than hold its own with bills of exchange based on currencies backed by immense accumulations of gold. The sterling prices of commodities proved more stable than gold prices. As an international currency, the paper pound gradually proved its superiority to the gold franc and the gold dollar. The London Money Market rapidly gained back its prestige. Britain very speedily established herself as the leader of a group of nations comprising half the world in a concerted effort to return to prosperity.

Meantime France and the United States continued their efforts to make the restoration of the gold standard utterly impossible, by fostering the use of gold for hoarding purposes rather than for currency. Britain ceased to perform the duties of debt collector for these countries on her withdrawal from the gold

standard, and they had accordingly to undertake the collection of their international debts themselves. This proved to be a task beyond the capacity of the United States, and the Hoover Moratorium was announced. This caused still further friction with France, as the latter country, though not included in the Moratorium, refused to pay her war debts, if Germany were to be allowed to postpone payment of her reparations.

France and her currency associates, Holland, Belgium, and Switzerland, proved more successful than the United States in denuding a distressed world of the last remnants of available gold. In 1931 these four countries absorbed between them £271 millions of gold, three times the amount of the total production from the gold mines of the world for that year. In 1932, there being less gold to drain, their absorption amounted to £244 millions only. These figures included not only the amounts placed to the reserves of the Central Banks; they also included large sums absorbed by private hoarding.

Hoarding on this scale not only destroys the possibility of the restoration of the gold standard for the present; it postpones to a far distant date even the consideration of the restoration of the gold standard. Before the gold standard could be restored, the practice of hoarding, now firmly established and rapidly on the increase, would have to be transformed into the habit of investing savings. Gold would also have to be freed from the hoarding mortgages that now cover the total monetary supplies of the world two

or three times over. Finally the hoarded gold would have to be disgorged in sufficient quantities to provide the basis of a world currency suited to the enormously enhanced production of the twentieth century. It is quite impossible to estimate the length of time that must elapse before such an improbable series of eventualities will occur. Long before that time can possibly arrive, the world will have ascertained that a far more effective international currency standard than gold can supply has been established, and is in actual working order, in a form that does not possess the handicap of being hoardable.

So chaotic was the economic condition of the world as the result of the breakdown of its system of currency, that a World Economic Conference was called in 1933 to see if some amelioration could be effected. By some mischance France, whose intensely national administration of the gold standard was largely responsible for the confusion that prevailed, was permitted to have a predominant voice in the preparation of the Agenda for the Conference. The success of the Conference was prejudiced in advance by the insistence of France that it must include proposals for the stabilisation of the foreign exchanges. *The Times* was able, in the leading article of its Special Gold Number, issued on June 20, 1933, to state that "one of the most important tasks of the World Economic Conference, which is sitting here in London, will be to prepare a way for the return to exchange stability through the rehabilitation of the gold standard."

President Roosevelt, elected to office at a time when the United States was passing through the worst financial crisis in its history, was greatly perturbed at the predominant French influence in the preparations for the Conference. He perceived that the United States would be pressed to subordinate its long established interpretation of stabilisation (of prices) to the European interpretation—the stabilisation of foreign exchanges. He forestalled this possibility and defeated the French manœuvres in advance by withdrawing the United States from what remained of the gold standard prior to the Conference.

The world thereupon divided itself naturally into three currency groups, a Sterling Group, a Dollar Group, and a Gold Group. With the two leading commercial nations of the world, Britain and the United States, off gold, all pretensions that the gold standard was a world international currency standard were dropped. Gold remained the nominal basis for commercial transactions on the Continent of Europe, but its use for the financing of sea-borne commerce almost vanished.

The World Economic Conference developed into a struggle between the United States and the nations of the Gold Group, with the nations of the Sterling Group seeking to find a formula of reconciliation between the contestants. But the differences between them were too fundamental to be reconciled by any formula. The countries of the Gold Group tried to force the United States to discard its own interpre-

tation of the term stabilisation, and to accept the European interpretation.

Never was an attempt more ill-timed or more certain of failure. Quite apart from the desperate position of the United States, the whole logic of the Macmillan Report and the whole force of the Currency Resolution of the Ottawa Conference, supported President Roosevelt's position. They both proclaimed that stabilisation of prices, not stabilisation of the exchanges, was the primary objective; and they both proclaimed that the time for stabilisation had not yet arrived, but must await the raising of the international price level to a satisfactory position of equilibrium. That was exactly the standpoint of President Roosevelt in his contest with the nations of the Gold Group at the World Economic Conference.

Twice they returned to the attack, and twice they were repulsed. The first attempt was made through the representatives of the Central Banks in attendance at the Conference. It received a firm but courteous negative. The second attempt was met with a scathing and contemptuous refusal, which demonstrated in a forcible manner that so far as the United States was concerned the gold standard was dead.

The gold standard was indeed dead in Britain, throughout the British Empire and the nations of the sterling group, and on the Continents of Asia and North and South America. As to the possibility and expediency of permitting its resurrection, the eminent Swedish Economist, Professor Gustav Cassel, states:—

> A return to the gold standard would be a hasty step, and certainly unfortunate. So long as the stability of gold cannot be relied upon, and so long as there is no assurance that the world's gold reserves will in future be exploited more rationally than hitherto, a return to the gold standard would be worse than a step in the dark; it would be a retrogression to an unworthy dependence on incalculable economic influences and political factors.

However dead the gold standard may be, efforts at resurrection are certain to be attempted unless and until some practical working alternative is not only suggested and expounded, but actually in operation. Fortunately, although the world appears to be in ignorance of the fact, such an alternative system is now actually in operation. The Currency Manifesto of the British Empire Delegates to the World Economic Conference, issued immediately after the Conference failed, informed the world that a new system of international currency had been initiated by the Commonwealths of the British Empire twelve months previously at the Ottawa Conference, that the new system was working satisfactorily, and that it had achieved a measure of success in the application of its policy. The system is a revolutionary system, based on the revolutionary proposals of the Macmillan Report. It is as revolutionary as the policy of President Roosevelt. It is in many respects a cautious and restrained variant of President Roosevelt's monetary activities. But though in its actual working it is cautious and restrained, in its ultimate objectives it is as revolutionary as the currency system initiated by Britain in 1816. It has

not attracted the attention which the more spectacular efforts of President Roosevelt have received, but it is working quietly, gradually, and efficiently. It is greatly assisting in restoring Britain's lost trade, reducing Britain's artificially induced unemployment, and raising Britain's commercial and financial prestige. The world in a short time will wake to the fact that a new sterling standard has been revived; a standard independent of the vagaries of gold, a standard incapable of being distorted by hoarding, a standard differing from, but as efficient as, the sterling standard of the nineteenth century. When this is realised the talk of restoring the gold standard will die through sheer inanity.

CHAPTER XII

THE STERLING-DOLLAR STANDARD

A New Working Currency

THE Currency Manifesto of the British Empire Delegates, issued on July 27, 1933, at the close of the World Economic Conference, is a declaration in effect that a new sterling standard, based on the lines quite as revolutionary as those which initiated the old sterling standard in 1816, had actually been established and was in active operation. Just as the old sterling standard had transferred the unit of value hitherto adopted from silver to gold, so the new sterling standard had transferred the unit of value from gold to an Index Number. In the twelve months during which the new standard had been working, it had achieved a substantial success towards the achievement of its main objective.

In deference to Mr. Neville Chamberlain, who presided at the Conference which issued the Manifesto, the customary tribute to the gold standard was offered, but it was worded in such a form that it may be regarded as an epitaph. It reads:—

> The undersigned delegations now reaffirm their view that the ultimate aim of monetary policy should be the restoration of a satisfactory international gold standard, under which international co-operation would be secured and maintained with a view to avoiding, as far as may be found practicable, undue fluctuations in the purchasing power of gold.

The use of the word "ultimate" is an assurance that so far as the working of the new standard is concerned, gold is to be ignored and kept out of the way for an indefinite and prolonged period. It is a recognition that gold is useless for any practical currency purpose at present. Some other standard is required to restore order out of the present chaos, and perform the active work of restarting prosperity. When that has been effected and the world can be assured that gold has lost its destructive powers ("undue fluctuations" is the euphemistic term employed) it may be permitted to be restored with safety as a subordinate monetary factor, somewhat in the position which silver occupies at present. The phrase "so far as may be found practicable" is a recognition of the fact that the growth of the habit of hoarding money may prevent the avoidance of "undue fluctuations in the purchasing power of gold." This qualification is an admission that it is highly problematical whether any return to gold will be feasible.

The main objective of the new currency standard, adopted by the Governments of the British Commonwealths is contained in the following passages:—

> The undersigned delegations are of opinion that the views they expressed at Ottawa as to the necessity of a rise in the price level still hold good, and that it is of the greatest importance that this rise, which has begun, should continue.

And:—

> They therefore consider that the Governments of the

British Commonwealths should persist by all means in their power, whether monetary or economic, within the bounds of sound finance, in the policy of furthering the rise in wholesale prices until there is evidence that equilibrium has been re-established, and that thereupon they should take whatever measures are possible to stabilise the position thus attained.

Stabilisation is here given its American interpretation, the stabilisation of prices and not of foreign exchanges. It is also prescribed that stabilisation is not an immediate possibility, but must be deferred "until there is evidence that equilibrium has been established." This is a complete endorsement of President Roosevelt's attitude towards the World Economic Conference. Perhaps the greatest value of the Manifesto of the British Empire Delegates is its demonstration that the main objective of the new British Currency Standard is identical with that of the currency policy of President Roosevelt. Britain has already adopted, and is operating, in a gradual and cautious manner, a currency standard which has the same main object as that which President Roosevelt is pursuing in a much more headlong and heroic manner. The possibilities of close and intimate currency co-operation between Britain and the United States, as soon as the different paces at which they are moving can be adjusted to each other, are very great, and suggest that the new sterling standard, now actually in operation, may in the not far distant future be transformed into a Sterling-Dollar Standard, based on identical interpretations of the term stabilisation, and of identical conceptions of the measures

by which it can be achieved. Co-operation with the United States will be as feasible on the new standard, as conflict was inevitable on the gold standard.

The identity of the new currency standard with the proposals of the Macmillan Commission, and the revolutionary nature of the changes its adoption has effected, can be judged from the following passage of the Macmillan Report:—

> Thus, our main objective should be, so far as it lies within the power of this country to influence the international price level, first of all to raise prices a long way above the present level, and then to maintain them at the level thus reached with as much stability as can be managed. We recommend that this objective be accepted as the guiding aim of the monetary policy of this country. The acceptance of such an objective will represent, in itself, a great and notable change. For, before the war, scarcely anyone considered that the price level could, or ought to be, the cause and pre-occupation, much less the main objective of policy, on the part of the Bank of England or the Central Banks.

This "great and notable change" has now become an actual fact. The first item "to raise prices a long way above the present level" is the accepted policy of "the Governments of the British Commonwealth." These Governments are not asked to adopt this policy. They are exhorted to "persist, by all means in their power, . . . in the policy of furthering the rise in wholesale prices." This is not a new policy recommended for adoption. It is an actually existing policy in full operation, to be persisted in "until there is evidence that equilibrium has been re-established."

The next problem to be faced is the equilibrium

level at which prices should be stabilised. This, being a matter for future determination, is at present a matter of conjecture. The Macmillan Report stated that "a large rise towards the price level of 1928 is greatly to be desired." President Roosevelt says—"Back to the price level of 1926." It is, of course, difficult to be precise because the exact answer will depend on the course of events in the meantime. But though it is difficult to be precise, both the Macmillan Report and the Currency Manifesto of the British Empire Delegates give very clear criteria by which to determine when the equilibrium price level shall have been attained. The former states:—

> A point will eventually come when, taking the world as a whole, international prices will have to be restored to a level which is approximate to the then existing levels of salaries and wages, and to the burden of monetary indebtedness.

The latter states:—

> Any price level would be satisfactory which restores the normal activity of industry and employment, which ensures an economical return to the producer of primary commodities and which harmonises the burden of debts and fixed charges with economic capacity.

The actual price level ultimately selected as the equilibrium level will be of the utmost importance, because it will provide the unit of value for the new standard, just as the price of £3 17s. 10½d. per ounce of gold provided the unit of value for the old sterling standard. This involves the substitution of a Price

Index for gold as the basis of the unit of value. This is foreshadowed by the Macmillan Report in the words:—

> The ultimate aim should be the stability of the international price level, meaning by this the composite price at wholesale of the principal foodstuffs and raw materials entering into international trade as measured by the best known wholesale index numbers.

Lord Bradbury's ironic prophecy that "the substitution of an index figure for gold as the standard of value" would not "come within the range of practical politics during the lifetime of the youngest of us" has already been falsified. Within a year from the date of the publication of his prophecy, in fact at the Ottawa Conference, a new system of currency was inaugurated requiring an Index Figure instead of gold as the standard of value for the currencies of the British Commonwealth.

The actual price index provisionally selected by the British Empire Delegates at the Ottawa and World Economic Conferences to measure the rise in prices towards the equilibrium point is the *Economist* Index, one of the oldest, most famous, and most reliable of price indexes. The operation of the new standard and the progress made towards the suggested equilibrium is explained in the following quotation from the Manifesto:—

> Taking the whole period from June 29, 1932, just before the assembly of the Ottawa Conference, a rise in sterling wholesale prices has taken place of 12 per cent, according to the *Economist* index. The rise in the sterling prices of

primary products during the same period has been much more substantial, being in the neighbourhood of 20 per cent.

The ignoring of gold and gold prices, and the association of sterling with a Price Index, in the above passage is not a mere accident. It is fundamental. Sterling withdrew from gold in September 1931, and became an inconvertible paper currency. In July 1932, at the official inauguration of a new monetary policy by the Ottawa Conference, sterling was deliberately associated with a policy requiring that its value should be measured by a Price Index; and a Price Index was selected to measure the rise in Sterling Prices, which was the main objective of the new policy. The object of a currency standard is to provide a measure of value. The measure of value of sterling prices adopted for the new Empire currency policy is a figure on a Price Index. Whether formally acknowledged or not, the *de facto* standard of British currency at the present moment is governed by the movements on the *Economist* Price Index.

The Ottawa Conference of 1922 did not, like the Macmillan Commission, merely make recommendations. It actually inaugurated a new currency policy. It started it working. According to the Currency Manifesto of 1933, the policy of the British Commonwealths since the Ottawa Conference "has been directed to raising prices" with the satisfactory result that, while gold prices were declining, sterling prices, measured on a Price Index, rose by 12 per cent and

20 per cent for wholesale goods generally and for primary products respectively.

The pound sterling is at present in a period of transition from an inconvertible paper currency towards a fixed standard. The rise in the Price Index, which under the newly adopted currency policy now governs its value, has not yet arrived at a satisfactory equilibrium point suitable for stabilisation. It is moving towards the position of equilibrium at which it can be stabilised, but has not yet arrived there. Until it reaches that point there can be no scientific standard of value. A scientific currency standard must have a fixed unit of value; in the case of a Price Index, a fixed point on the Index. Until the time comes for stabilisation, the pound sterling itself, at whatever figure the price level may happen to be, is the standard of value. It is unsatisfactory having a movable basis of this nature as the standard, but it is inevitable in a period of transition. Exactly the same kind of movable standard was necessary in the period of transition, 1816–22, until the sterling price of gold was attained and fixed. A pound sterling of a movable value is far less erratic as a currency basis than the value of gold. Its movements are controlled, and it is moving in a predetermined path towards a definite objective. A standard of value of this nature, though not strictly scientific, is open to less objection than any other standard. The pound sterling, moving at a steady pace towards a fixed equilibrium, is the best standard the world has known since 1914.

The Currency Manifesto of 1933 does not contemplate a merely passive attitude until the point of equilibrium on the Price Index suitable for stabilisation shall be attained. An active policy "to reconcile the stability of exchange rates with a reasonable measure of stability of prices" is immediately possible. Such a reconciliation can be effected at once between the countries of the Empire. Its "achievement will be aided by the pursuit of a common policy of raising price levels." The Manifesto is most emphatic that no stability of exchanges can be satisfactorily achieved except on the basis of the pursuit of a common policy of raising price levels. In order that the new Imperial currency policy may have a chance of success there must be "no commitments to other countries as regards the future management of sterling." Stability of the exchanges must be subordinate to a common policy of stabilisation of prices. There must be no possibility of the new system of currency being wrecked by internecine conflicts of the nature of those which wrecked the gold standard between 1925 and 1931. No stabilisation of the exchanges is to be effected with any country except on the clear understanding that the Imperial policy of price stabilisation is accepted, and will be adopted.

But, provided that other countries are willing to adopt and operate a policy on similar lines, they will be welcomed into the group, and their inclusion "would make possible the attainment and maintenance of exchange stability over a still wider area." Stability

of exchange with sterling is to be regarded as a privilege and not as a right. It is to be an inducement to all countries willing to co-operate with the British Empire in the restoration of world prosperity. It is not to be permitted to countries whose currency policies are of such an intensely national character that they tend to wreck any international currency system with which they are associated.

The members of the Sterling Group of Nations have been bitterly disappointed at the repeated declarations by responsible British statesmen of adherence to the gold standard. They cannot understand the typical British procedure by which momentous revolutions are effected under cover of the pretence that nothing has been changed. They refused to believe "the great and notable change" proposed in the Macmillan Report because it was associated with adherence to the gold standard. They refused to believe that the Ottawa Conference actually set up a new working system of international currency for the same reason. But the British Empire Delegates Currency Manifesto of 1933, despite a similar handicap, made a different impression. It did not invite them to come to a conference. It invited them to come in to an actually working system of international currency, free from the disturbing influence of the franc and the dollar, a currency as near as possible as the altered world conditions will permit, to the sterling standard under which they had flourished before the war.

They are hesitating. They still distrust the Bank of England with its pro-French administration of the Exchange Equalisation Account. They distrust still more the critical attitude of British financial interests towards President Roosevelt's efforts to achieve currency reform. But as the realities of the new Imperial currency system become more widely known, there is no doubt that they will accept an invitation to join a currency system so closely in harmony with their own interests.

An example of the bewilderment caused in the Sterling Group of countries by their uncertainty as to the future course of British currency policy, is to be found in an article in the *Monthly Review* of Barclays Bank for November 1933, advocating "closer collaboration with the gold standard countries." Such a recommendation is in distinct defiance of the Imperial currency policy prescribed in the Currency Manifesto of 1933, which states:—

> Inter-Imperial stability of exchange rates is facilitated by the fact that the United Kingdom Government has no commitments to other countries as regards the future management of sterling and retains complete freedom of action in this respect.

Yet the official review of one of the leading British Banks advocates a policy which would jeopardise Inter-Imperial stability of exchange rates by close collaboration with the gold standard countries, whose currency policy is diametrically opposed to what is now the official policy of the Empire. For purely

British purposes, it may be satisfactory to pretend that we have not already effected a complete revolution in our currency system. But if the Sterling Group is to be established as the next objective towards the final realisation of a new international currency system, it is imperative that there should be a correct appreciation of what our present currency system is, and consistency in all authoritative references to it.

There remains the problem of the United States. At the time of writing, the financial world has just been shaken to its foundations by the currency proposals of President Roosevelt contained in a speech broadcast on October 22, 1933. It is difficult to appreciate what all the bother is about. There is nothing in the portions of his speech available that might not have been taken from the Manifesto which proclaims the official currency policy of the Governments of the British Commonwealth. President Roosevelt appears to have proposed nothing that has not been proclaimed in much more forcible terms as being the actual working currency policy of the British Empire. A comparison may be instituted between the principal proposals he has made, and those set forth in the British Currency Manifesto. It will be seen that they show the British system as the more revolutionary of the two.

President Roosevelt proposes "a managed currency." The British Manifesto prescribes "the deliberate management of the international standard."

President Roosevelt's declared objective is "to

restore the price level first." This is the actual official currency policy of the British Empire, and has been in operation since the Ottawa Conference. The British Manifesto records "with satisfaction that this policy has been attended with encouraging success."

President Roosevelt says that "it may be necessary from time to time to control the gold value of the dollar." The British Manifesto goes further. It does not seek to control, it ignores the gold value of sterling, and associates sterling with a Price Index instead.

President Roosevelt says that the dollar is "altogether too greatly affected by the accidents of international trade, by the internal policies of the nations, and by political disturbances in other Continents." The British Manifesto, in full agreement, says "no commitments to other countries as regards the future management of sterling," "complete freedom of action in this respect," and no exchange stabilisation with any country unless it adopts a price policy similar to ours.

President Roosevelt seeks "to establish and maintain a dollar which will not change its purchasing and debt-paying power during the succeeding generation." The British Manifesto states that "a price level would be satisfactory which harmonises the burden of debts and fixed charges with economic capacity."

In addition President Roosevelt has copied the British example and established exchange control by a method similar to that of the Exchange Equalisation Fund.

The Times Washington Correspondent exclaims

"his Conservative hearers last night were aghast." *The Times* leader states:—

> There are certainly ambiguities, and even what would appear to be contradictions in the speech, as it has been reported in this country.

Judging the portions of the speech actually reported in *The Times*, there was nothing in it to make anyone aghast, no ambiguities, no contradictions. It contained nothing that had not been recommended by the Macmillan Commission, nothing that had not been authorised by the Ottawa Conference, nothing that is not the actual working policy of the Governments of the British Commonwealths according to the British Currency Manifesto of 1933.

The commotion caused by President Roosevelt's currency proposals indicate the magnitude of the silent revolution which has been effected in British currency policy since the Ottawa Conference. If the mere broadcasting of a few of the outstanding features of that policy has created such a stir in the United States, Britain is to be congratulated on having proceeded further on the road towards progress and prosperity without being even conscious that any movement had been made. The reforms characterised by the Macmillan Commission as "a great notable change" have been effected in the traditional British manner, without anybody appreciating that anything out of the way has happened.

For the time being the progress of the new system of currency will comprise the raising of the sterling

price level on the *Economist* Price Index towards the equilibrium point, and the stabilising of the exchanges with all members of the sterling group. Meantime the United States will be proceeding on parallel lines by raising the dollar price level. The pursuit of a common objective by such a powerful commercial organisation as the Sterling Group, informally and effectively assisted by the co-operation of the United States in moving towards the same objective, will probably result in complete success, especially as progress will not be trammelled by the operation of an obsolete currency system.

The critical time will arrive when the stabilisation point is being approached. There will probably be many differing points suggested for adoption. A conference will be necessary to arrive at a decision. The conference will include all the nations in the Sterling Group; and undoubtedly the United States, with a similar price stabilisation policy, will be invited to participate. The conference will not be called to discuss some unwieldly and amorphous subject like the return to prosperity. It will have one object, and one object only, that of selecting a figure on the approved Price Index to be adopted as the future standard of value. The advantages of a common standard for the Sterling Group and the United States will be so obvious that the pound sterling and the dollar will probably be stabilised on the same unit of value.

The Price Index chosen for fixing the unit of value will probably be the Production Index of the League

of Nations. The compilation of this Index is based on the commercial axiom that the price of every commodity on the high seas, freed from the disturbing factors of cost of transport and tariffs, is the same for every currency and every country in the world. The disturbing factors are eliminated by recording the prices on shipment at the ports of the exporting countries. The compilation of the weighted average price of the principal primary commodities in general demand in this manner, gives a wholesale Price Index uniform for the whole world. It is the most natural measure of value that the ingenuity of man has devised. It is the obvious basis for the fixation of an international scientific unit of value.

Once the particular figure to be the standard of value for the international currency had been fixed and adopted, it would be maintained by exactly the same methods which were adopted by the Bank of England to keep the price of gold fixed at the value of £3 17s. 10½d. per ounce for ninety-two years. A certain amount of play, probably half a point above and below the fixed standard, would be permitted. If the price level tended to move outside these restricted limits, the minor methods of control to counteract such movement would first be applied. If these proved ineffective, the major and more powerful methods of control would be applied till the price level returned to the equilibrium point.

The methods adopted would be the traditional methods of the expansion and contraction of currency

and credit. Should prices tend to rise above the equilibrium point, it would indicate that credit and currency were over supplied, and restrictive measures would be enforced to the extent necessary. On the other hand, should prices tend to fall, expansive measures would be adopted. The measures in both cases would be reflative, that is, tending to bring the price level back to the position of equilibrium.

Gold would still be required (silver might also be used) to settle international balances, under the new currency standard. But the movements of gold would not cause the price distortion they have produced in the past. The prices of commodities would be completely divorced from the value of gold. The price of gold would be determined by the demand for hoarding, for currency, and for the arts, relative to the supply. As long as hoarding continues at its present pitch of intensity the price of gold will remain high. But, as confidence increases and the habit of investment grows, hoarding will gradually diminish, and the price of gold will fall.

The demand of gold for currency purposes will be relatively greater for high protection countries than for Free Trade or low protection countries. With an assured price level and increased confidence, the high protection countries will probably invest the surplus gold they receive with the debtor countries. Otherwise their protection policies will impose upon them a serious commercial handicap. Instead of exporting goods they will be accumulating gold at highly un-

remunerative prices. So long as the hoarding complex remains dominant, gold will be accumulated both by individuals and by Central Banks, but at extremely high prices. When it is realised that gold is but an unimportant factor in international trade, and that no country can be forced (as Britain was in 1930–31) to sell gold below its market value, the urge for large accumulations may be expected to diminish in intensity.

Assuming that the success attending the initial operations of the new currency policy based on price stabilisation continues, it is difficult to visualise the circumstances under which a return to the gold standard could possibly be attempted. It would be impossible to repeat the furtive method by which the gold standard was imposed on Britain in 1925. The present currency policy is an Imperial Policy, adopted at the Ottawa Conference of 1932, and subsequently expanded and confirmed by the Currency Manifesto of the Imperial Delegates issued after the failure of the World Economic Conference of 1933. By the time world economic conditions have become so stable that a return to gold might be contemplated, the present policy would have established itself not only as an Imperial Policy, but as a successful policy. It could not possibly be discarded and a return to gold effected, without such decisions being formally adopted at an Imperial Conference after lengthy preliminary discussions. To change an Imperial currency policy, especially an Imperial policy which had operated suc-

cessfully for some years, for an alternative policy with an extremely questionable record, would be a proposal so revolutionary and so astonishing that it would require remarkably convincing arguments to ensure its acceptance. Moreover, a return to gold would be a breach of faith with the nations of the Sterling Group.

A proposal to return to gold would encounter a series of obstacles almost certain to prove insurmountable. It has already been condemned unanimously by the Conservative Party. The Labour Party is quite as unanimous and much more bitter in its opposition. The Federation of British Industries was strongly hostile to a return to the gold standard in 1924, much more determined in its hostility to its operations in 1931; and its future opposition would be reinforced by bitter memories of solemn warnings contemptuously flouted, and prophecies of ruin more than fulfilled. Every employer and every worker in every mill, factory, mine or warehouse in the country would unite as one man in opposition to a return to a currency standard associated with the humiliations, the losses, and the disasters of the six years, 1925–31.

In meeting this implacable opposition, the Government would be confronted with the paradox that they would be asking the Empire to go back to the gold standard, under which it had been brought to the brink of disaster, and to forsake a currency standard which had rescued the Empire from that critical position and brought it back to prosperity. Gold is to be discarded for the present as a faithless ally, a

burdensome handicap, a treacherous support, and a dangerous associate during the years of struggle from humiliation and disaster to confidence and prosperity. But when the moment of victory arrives, the currency policy and the currency standard which have borne the brunt of the uphill fight, and have been instrumental in achieving the victory, are to be discarded as unworthy of further confidence, and the unstable and inconsequent weakling which was found wanting and was discarded in the time of peril, is to be garlanded in triumph and restored to favour and supremacy.

Even if circumstances can be imagined as being propitious at some future date for a return to gold, it is difficult to conceive that a currency system, which has proved its success by bringing back the world to prosperity will be abandoned, in defiance of the wishes of the whole nation, for a system which has already proved a signal failure. But is it possible to anticipate that in the future conditions will be any more propitious for a return to gold than they are at present, or than they were in 1931? Will the present craze for hoarding, fostered by nineteen years of conditions stimulating a return to this primitive habit, suddenly change and release gold in volumes adequate to provide a basis for a world currency? With the return of confidence to the world, the practice of investing savings instead of hoarding them may be expected gradually to return. But long before the change operates sufficiently to release enough gold to restore

the gold standard, the gold standard will have been forgotten.

Or, will those Central Banks, which have accumulated three quarters of the monetary gold of the world, consent to distribute their hoards equitably throughout the countries of the world, in order that an international currency system similar to the sterling standard of the nineteenth century may be established? It is now eleven years since the Genoa Conference recommended co-operative action between the Central Banks to regulate the price and the distribution of gold as a preliminary to the return to the gold standard. The prospects of such co-operation are much less now than they were then. There is now less internationalism and more nationalism in the attitude of the gold-holding nations than there was in 1922. If the restoration of the gold standard depends on a more equitable distribution of gold, the history of the past eleven years shows that it can be ruled out as an eventuality that has no prospect whatever of being realised.

Or, again, is there any likelihood of France and the United States changing their tariff policies so that the International Balance of Trade can be effected by means of goods and services independently of gold, as under the pre-war sterling standard? The disastrous manner in which their protective policies affected British industry (under the gold standard) as explained in Chapter VIII, would again have an exactly similar effect if the gold standard were restored. Both France

and the United States regard their tariff policies as being of much greater importance to them than the working of an international currency standard, and there is no likelihood whatever of their effecting a change which would revolutionise their traditional fiscal policies in order to make a gold standard workable.

Or, is it possible to visualise a change in the currency mentalities of Britain, France, and the United States, that would avoid the conflicts which raged between their currency policies from 1925–31, and permit of a co-operative working of the gold standard? There has certainly been one remarkable change in the respective currency mentalities of Britain and the United States in the past two years. But that has operated adversely to a return to a gold standard, and not in its favour. The Macmillan Report recommended that Britain should accept the American conception of stabilisation, that is a stabilisation of prices, as the main objective of its currency policy. This recommendation has now been adopted both by the Ottawa Conference and by the British Imperial Currency Manifesto of 1933, and is at present the actual working policy of the British Empire. It renders currency co-operation between Britain and the United States possible, but not on a gold standard. Quite apart from the protective policy of the United States which prohibits currency co-operation between the two countries on the gold standard, price stabilisation can only be effected satisfactorily on an Index Standard.

There are thus four serious obstacles to be overcome before a return to the gold standard can even be contemplated. These are: hoarding, the maldistribution of gold, the protective policies of France and the United States, and the precedence now accorded to stabilisation of prices over stabilisation of the foreign exchanges. Even in the highly improbable contingency that these four obstacles could be negotiated, there would then remain the further problem of finding some logical reason for the paradox of forsaking a proved and established successful currency standard for another which was dis-established because of the disasters it brought upon the world. This paradox will have to be forced upon an intensely unwilling and bitterly hostile country before it can be included in the Agenda of the Imperial Conference called to make the decision. Finally will come the supreme task of persuading the Dominions of the British Commonwealth to put the clock back, and to return to a currency standard which they distrust even more heartily than it is distrusted in Britain.

It is a comparatively easy task to get their permission to interpolate a pious paragraph of respect for the gold standard, rendered nugatory by such expressions as "ultimate" and "as far as may be practicable" in a Manifesto effecting a complete breach with the gold standard. But it will be a task of a very different nature to persuade them to forsake a successful standard, actually in operation, a standard which has brought them back to prosperity, and to adopt in its

stead a discredited standard with a dismal record of failure.

The attitude of the United States will be an important factor in Britain's consideration of a return to a gold standard. Britain and the United States will presumably for the next year or two be pursuing parallel paths towards the identical objectives of a rise in prices to some equilibrium level, and then the standardisation of prices at that level. This will involve a certain amount of co-operation for which both Britain and the United States are ready and willing. Having succeeded in achieving prosperity by active co-operation towards identical objectives, will Britain in the moment of success suddenly cease co-operation and embark on a contradictory gold standard policy that will mean a certain conflict with the United States and a reversal of all the benefits that co-operation has achieved?

Britain's return to the gold standard is therefore linked up with the possibility of the return of the United States to the gold standard. The experience of the United States of the working of the gold standard from 1929 to 1933 was even more bitter and more disastrous than that of Britain from 1925 to 1931. The gold standard does not fit in with the American conception of stabilisation—stabilisation of prices. The value of gold is much too unstable a standard by which to measure stability of prices. The recent fluctuations in the price level of commodities have been due, primarily, to the instability of gold.

Stabilisation of prices requires the greatest possible stability in the currency standard, and this can only be achieved on a price index. When the Macmillan Report recommended that Britain should make price stability its main objective, it implied (as Lord Bradbury pointed out) the adoption of an Index Standard as the standard of currency. This is clearly acknowledged in the United States, and a return to gold is now practically unthinkable for that country. Co-operation towards the same objectives and practical experience in achieving stabilisation, in the modified meaning of that term, will gradually create the same opinion in Britain.

It is necessary that the reality which lies behind the superficial phrase "the restoration of the gold standard" should be appreciated in its true perspective. On the one hand, the advocates of such a restoration should appreciate that it cannot be accomplished by a mere declaration that for the future gold will be the standard of British Currency. The course they are advocating will lead to an industrial and commercial strife of an unpredictable bitterness. Both employers and workers are now aware that the operation of the international currency standard has a much greater effect, whether adverse or beneficial, than the operation of Free Trade or Protection. The acerbities of the conflict between these two fiscal policies will be transformed and magnified to a much greater intensity, should a struggle between two rival currencies become the primary political issue. A declaration in favour of a return to

the gold standard is in fact a declaration of war against the currency standard that is slowly bringing Britain and the world back to prosperity.

Moreover, the traditional British method of effecting revolutions in substance while retaining outward forms unchanged is not understood by those nations which are willing to work cordially with Britain in making her currency policy effective, if only they are certain what her policy is. Every declaration by a prominent financier in favour of "the restoration of the gold standard" is a suggestion to the other nations that Britain does not know her own mind, that she is doubtful of the wisdom or the success of her present currency policy, and that any nation that joins up with her may in future be left in the lurch when Britain goes back to gold. Clearly and authoritatively defined as British currency policy now is, successfully as it is operating, it can never secure complete confidence throughout the world until it has achieved an absolute break from the gold standard. The break must be as clear as the break of the sterling standard from the old silver standard in 1816, if the international success of the old sterling standard is to be repeated.

The country has not yet grasped the nature of the new currency policy of the British Empire. But the country has grasped that it is producing diametrically opposite results to those produced by the gold standard from 1925 to 1931. The present currency policy is producing prosperity, not disaster; it is diminishing unemployment, not creating it; it has restored British

prestige, not made the name of Britain a by-word among the nations; it has renewed the self-confidence of all sections of British Industry, not destroyed it with handicaps and burdens grievous to be borne. A system of currency is judged, not by the theoretical conceptions of the bank parlour, but by the practical results in the market place. Judged by that criterion, the gold standard is damned for ever. Its restoration in the place of a system which has restored confidence and prosperity will be about as practicable as the restoration of the feudal system.

The return to prosperity requires no further World Economic Conference. The return is actually in progress. Industry requires no further currency revolution. The revolution has actually been effected, all the more thoroughly because it has been effected in the traditional, silent, inconspicuous British manner. Any statesman who would deliberately intervene to interrupt the steady progress towards prosperity by tampering with the now established system of English currency which is functioning so admirably would experience a hundredfold the bitter resentment now felt towards those responsible for the restoration of the gold standard in 1925. Fortunately, it is improbable that any statesman will ever have the opportunity to propose that such a step should be taken. Every day that the existing system functions will strengthen its hold on Britain, on the Empire, and on the World, and render an attempt to put the clock back an extremely dangerous proceeding for anyone contemplating such an action.

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